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No. 84-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

TRANSCONTINENTAL GAS PIPE LINE CORPORATION,
Appellant,

VS.

THE STATE OIL AND GAS BOARD OF MISSISSIPPI AND COASTAL EXPLORATION, INC., *et al.*
Appellees.

On Appeal from the Supreme Court of Mississippi

JURISDICTIONAL STATEMENT

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QUESTIONS PRESENTED

1. By enacting the Natural Gas Policy Act of 1978 did Congress intend to cede to the states its preemptive jurisdiction over interstate pipelines and their purchase and transportation of natural gas for resale in interstate commerce, thereby overruling *Northern Natural Gas Co. v. State Corporation Commission* 372 U.S. 84 (1963)?

2. Does Mississippi's attempted regulation of interstate pipeline companies' purchase of "high cost" gas constitute an impermissible burden on interstate commerce under present market conditions?

PARTIES TO THE PROCEEDING

In addition to the parties named in the caption, Wiley Fairchild, Rodney Fairchild, W. R. Fairchild Construction Company, Ltd., Getty Oil Company, Inexco Oil Company, and Tomlinson Interests, Inc. are producers who have appeared in opposition to Transcontinental Gas Pipe Line Corp. at all stages of the proceedings.

The following persons personally appeared before the Mississippi State Oil and Gas Board at the initial proceeding:

Susan W. Clements Lay
Lane Petroleum Corp.
Louis G. Ridgeway
Daniel E. Herlihy
Bryant M. Allen

Transcontinental Gas Pipe Line Corporation is a wholly-owned subsidiary of Transco Energy Company. Affiliates of Transcontinental Pipe Line Company are Border Gas, Inc. and NESP Supply Corp.

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On Appeal from the Supreme Court of Mississippi

JURISDICTIONAL STATEMENT

Transcontinental Gas Pipe Line Corporation (Transco) makes this appeal from the judgment of the Mississippi Supreme Court, entered on September 5, 1984, upholding a regulation and order of the State Oil and Gas Board of Mississippi in the face of federal constitutional challenges. Transco submits this statement to show that the Supreme Court of the United States has jurisdiction over the appeal and that a substantial question is presented.

OPINIONS BELOW

The opinion of the Mississippi Supreme Court (App. A, *infra*, 1a-58a) is reported at 457 So.2d 1298 (Miss. 1984). The

opinion of the Circuit Court of Hinds County, Mississippi (App. B, *infra*, 59a-103a) is not reported. The order of the Mississippi State Oil and Gas Board (App. C, *infra*, 104a-113a) is not reported.

JURISDICTION

This case involves a challenge to the constitutionality of Statewide Rule 48 of the State Oil and Gas Board of Mississippi. The Mississippi Supreme Court entered its judgment upholding the challenged regulation and order on September 5, 1984. (App. E, *infra* at 115a). A petition for rehearing was filed by Coastal Exploration, Inc. and was denied on October 5, 1984. (App. D, *infra* at 114a). Transco filed a notice of appeal to this Court on November 30, 1984 (App. F, *infra* at 116a). The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(2). *Atchison, Topeka & Santa Fe Railway Co. v. Public Utilities Commission*, 346 U.S. 346, 348 (1953).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The pertinent provisions are set forth in App. G, *infra*, 119a-129a.

STATEMENT OF THE CASE

Greens Creek Field and East Morgantown Field are two separately defined natural gas fields in Marion County, Mississippi. Greens Creek Field was discovered in 1976. The Harper Sand of that field was first encountered in 1978. Approximately five miles south of the Greens Creek Field, the East Morgantown Field was discovered. Its Harper Sand was discovered in March of 1979. In 1980, Getty Oil Company discovered additional Harper Sand production directly between these two fields with its Rogers 28-11 Well No. 1. As a result of this discovery, five additional wells were

drilled around the Rogers 28-11 No. 1. Some of these wells were within the area designated as the East Morgantown Field and some were in the Greens Creek Field, although all were producing from a common Harper Sand Gas Pool. All production from the Harper Sand of these two fields was below 15,000 feet and, thus "high cost gas" under § 107 of the Natural Gas Policy Act of 1978 (NGPA).[1]

Transco purchases gas and transports it from fields in Texas, Louisiana, Mississippi and the federal off-shore domain for resale to its customers along the pipeline extending from Texas to New York. It is a "natural gas company" under the Natural Gas Act and an "interstate pipeline" under the NGPA.[2] Transco had contracted with and had been purchasing gas from producers in the Greens Creek Field since 1978. On the basis of the reserves committed to it under those long term contracts, Transco had extended its pipeline facilities to that field. When the East Morgantown Field was discovered, Transco also entered into long term contracts with producers and, as a result thereof, extended its pipeline facilities to those wells in order to recover the dedicated reserves. When the Harper Sand Gas Pool production between these two fields was discovered in 1980, Transco already had some of that area dedicated under its prior contracts. Transco began taking gas under these contracts and entered additional contracts with other producers to cover their production.

By early 1982, Transco had approximately 35 different contracts with various producers in these two fields. Because these contracts were entered into at various times with different producers, there was a substantial difference in the contract terms. The principal differences involved the

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[1]15 U.S.C. § 3317.

[2]15 U.S.C. § 717(b); 15 U.S.C. § 3301 (15).

price to be paid for gas and the quantity of gas which Transco was to purchase or pay for.

Transco, like every other interstate pipeline, had faced a severe shortage of available reserves and curtailment of its resales customers during the 1970's. As a result of the seller's market which prevailed while Transco competed for new reserves, some of the gas purchase contracts with producers in these fields contained provisions calling for Transco to take as much as 100% of the amount of gas which could be delivered from any well. In later contracts, the "take-or-pay" provisions called for Transco to take between 80 and 90% of the contract seller's deliverability in a well.[3]

The operators of the six wells in this pool each had a contract with Transco. However, not all of the producers in the Harper Sand Gas Pool entered into contracts with Transco. Many producers, like Coastal Exploration, Inc. (Coastal), did not have contracts but had elected to let the operator sell gas for their account under an operating agreement.[4]

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[3]A "take-or-pay" provision is the most common form of minimum-quantity requirement in natural gas contracts. *See, e.g.*, Energy Information Administration, U.S. Dept. of Energy, *Structure and Trends in Natural Gas Wellhead Contracts* vi, 29-38 (1983) (hereinafter cited as EIA); H. Broadman and W. Montgomery, *Natural Gas Markets After Deregulation* 7 (1983) (hereinafter cited as Broadman). The provision typically requires a pipeline to either accept deliveries of natural gas and pay for it or pay for it with a right to accept delivery within a specified "make-up" time, usually several years. Under federal regulation, take-or-pay payments for gas not currently taken are capitalized and a return thereon is allowed to be charged to the consumer.

[4]An operating agreement is the usual means in the oil and gas industry of defining the rights and duties of an operator, *vis-a-vis* the nonoperating owners, as to the drilling and production of a well. In this case, every well involved in this dispute was covered by a form

Other producers had rejected contract offers by Transco but had failed to make arrangements to otherwise dispose of their gas. Still other producers in these wells had entered into contracts with another interstate pipeline company which, at the time of the Board hearing, was not taking any gas from the wells and had refused to purchase Coastal's gas.

Prior to the spring of 1982, Transco had sufficient market demand to take all volumes of gas tendered to it, both contract gas and the gas sold under operating agreements for the account of non-contract parties. However, in the spring of 1982, Transco began to experience problems in reselling the gas on its system. Transco's average cost of natural gas had significantly increased over the last two years because of the price increases and escalations allowed under the NPGA and because of the operation of contract pricing provisions applicable to price deregulated high cost gas.[5] Meanwhile, prices for alternate fuels were actually dropping. As a result, some industrial customers switched to cheaper fuel oils.

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operating agreement which provided that (1) each party was to take in kind or separately dispose of its proportionate share of the oil or gas produced from the well and (2) in the event such party did not make arrangements necessary to take in kind or separately dispose of its share of oil or gas, the operator then had,

> the right, . . . but not the obligation, to purchase such oil and gas or sell it to others at any time from time to time, for the account of the non-taking party at the best price obtainable in the area for such production . . . only for such reasonable periods of time as are consistent with the minimum needs of the industry under the particular circumstances but in no event for a period of in excess of one year.

[5]In the spring of 1982, Transco's system-wide average cost of gas was $3.13/MMBtu. This was over 82% of Transco's average resale price of $3.78/MMBtu.

By May, 1982, Transco had lost resale markets for approximately 95-100 million cubic feet of gas per day. Transco was unable to take or sell all of the gas subject to the take-or-pay provisions of its gas purchase contracts. Because the cost of wellhead purchases was continuing to escalate, Transco projected an additional $.65-$.70 increase in its average cost of gas. This would result in inevitable loss of additional markets. Since Transco was experiencing market loss at its distribution end and was projecting further losses, it invoked contractual provisions allowing price or quantity reductions and asked its sellers for voluntary reductions in both prices and quantity obligations.[6] It also notified all of its contract producers that it would no longer purchase any gas that it was not contractually required to purchase.

This announcement had varying impacts on Transco's purchases from different wells because of the different terms and conditions of its contracts. Some producers had bargained for specific agreements in their contracts requiring Transco to take all gas produced from their wells, regardless of ownership. However, other contract parties had not made those arrangements and, under their contracts, Transco was only obligated to buy gas owned by that particular seller. Coastal had no contract to sell its gas and there were no contracts obligating Transco to take Coastal's gas from some of the Harper Sand wells.

On July 29, 1982, Coastal filed a petition with the Mississippi State Oil & Gas Board (Board) under the Board's Statewide Rule 48. The petition sought to force Transco to purchase Coastal's gas on the same terms and conditions

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[6]Even with this effort, Transco was paying between $5.00 and $9.054 per MMBtu for the "Harper Sand" gas under contract from these fields. These prices were far greater than what Transco could resell gas for.

under which Transco was purchasing gas (under contract) from the well operators.[7] Rule 48 states:

> Each person now or hereafter engaged in the business of purchasing oil or gas from owners, operators, or producers shall purchase without discrimination in favor of one owner, operator, or producer against another in the same common source of supply.

Transco, by written response to the Board, challenged the proceeding on a variety of state grounds and also urged that the Board's attempted regulation of an interstate pipeline was preempted by federal regulation, under the Supremacy Clause, U.S. Const. art VI, § 2. On October 13, 1982, the Board rejected all of Transco's challenges and entered its Order No. 409-82 finding Transco in violation of its Rule 48, and directing it to,

> ratably take and purchase gas without discrimination in favor of one owner, operator or producer against another in the said common source of pool [sic]. . . .

App. C, *infra* at 112a.

At no time in the proceedings did the Board consider reducing well allowables to accommodate the reduced market demand or establishing allowables on anything other than the wells' maximum deliverability. Though subtly couched, the Board's Order had the practical effect of forcing Transco to take quantities of high cost gas it had no contractual obligation to take and, therefore, reducing its takes of lower priced regulated gas from other fields.[8]

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[7]The specific contracts under which Coastal was trying to force Transco to purchase its gas then called for a price of $7.90/MMBtu.

[8]The practical effect was created by the combination of the order, the acknowledged gas glut and the take-or-pay provisions in Transco's contracts. The result is an increase in its system costs which pass through to the consumer.

Transco appealed this order to the Circuit Court of the First Judicial District of Hinds County, Mississippi. Among its nine grounds of appeal, Transco contended that Board action was invalid under the Commerce and Supremacy Clauses of the Constitution. On June 28, 1983, the Circuit Court considered every assignment of error and affirmed the Board's order in its entirety.

Thereafter, Transco appealed to the Mississippi Supreme Court. On September 5, 1984, that Court entered its 58 page opinion rejecting Transco's position on all federal constitutional issues. However, the Mississippi Supreme Court found that the Board's attempt to regulate or proscribe differences in price, although constitutional, was not within the Board's statutory authority under Mississippi law.

On October 3, 1984, the Mississippi Supreme Court overruled a petition for rehearing filed by Coastal.

THE QUESTIONS ARE SUBSTANTIAL

I. Are State "Ratable-Take" Regulations Still Pre-Empted by Federal Regulation of Natural Gas Purchased and Transported for Resale in Interstate Commerce?

The State Oil & Gas Board of Mississippi has, in this case, attempted to revive a "ratable take" regulation admittedly unenforceable as to interstate pipelines prior to 1978. Oklahoma[9] and Texas[10] are now revising their ratable take regulations to be enforceable against interstate pipeline companies. The validity of this recent state assertion of jurisdiction hinges on the true scope of the decision reached in *Northern Natural Gas Co. v. State Corporation Commission*, 372 U.S. 84 (1963).

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[9]See App. H, *infra*, at 130a-135a.

[10]See App. I, *infra*, at 136a-152a.

The Mississippi Supreme Court and producers in this case concede that *Northern Natural* would be dispositive but for the Natural Gas Policy Act of 1978 (NGPA).[11] However, they contend that since § 601(a)(1) of the NGPA has eliminated regulation under the Natural Gas Act[12] over the "first sale" of "high cost gas," an interstate pipeline's purchase of this gas is free from federal control and therefore subject to state regulation. This tunnel vision approach simply does not take into account the scope of federal jurisdiction over pipelines under the Natural Gas Act and the NGPA. It does, however, raise the substantial question of whether Congress, by "deregulating" prices of first sales of certain categories of natural gas, intended to allow states to regulate the quantity and price of gas purchased by an interstate pipeline and transported for resale in the interstate market.

1. The Natural Gas Act was enacted in 1938. It gave the Federal Power Commission (Commission) three independent bases of jurisdiction: (1) over "transportation of natural gas in interstate commerce"; (2) over "sales for resale in interstate commerce;" and (3) over "natural gas companies engaged in such transportation or sale." 15 U.S.C. 717(b).

Although Congress placed specific limitations on the Commission's jurisdictions over rates, the jurisdiction over transportation, and incidents of transportation, has not been construed so narrowly. *Compare Panhandle Eastern Pipe Line Co. v. Public Service Commission*, 332 U.S. 507 (1947) (rates of direct sales) *with FPC v. Louisiana Power and Light Co.*, 406 U.S. 621 (1972) (quantities of direct sales). "Where it is necessary to regulate the purchase of gas in some respects to carry out its expressly granted au-

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[11]15 U.S.C. § § 3301-3432.

[12]15 U.S.C. § § 717-717w.

thority over transportation and sales, the Commission must have the power to do so." *United Gas Pipe Line Co. v. FPC*, 385 U.S. 83, 90 (1966).

In *Northern Natural*, this Court found Kansas ratable take orders preempted because they invaded the exclusive jurisdiction "which the Natural Gas Act has conferred upon the Federal Power Commission over the sale and transportation of natural gas in interstate commerce for resale." 372 U.S. at 89. The "imminent possiblity" of conflict was deemed sufficient to preempt state regulation:

> The danger of interference with the federal regulatory scheme arises because these orders are unmistakably and unambiguously directed at *purchasers* who take gas in Kansas for resale after transportation in interstate commerce. In effect, these orders shift to the shoulders of interstate purchasers the burden of performing the complex task of balancing the output of thousands of natural gas wells within the State, . . . a task which would otherwise presumably be the State Commission's. Moreover, any readjustment of purchasing patterns which such orders might require of purchasers who previously took unratably could seriously impair the Federal Commission's authority to regulate the intricate relationship between the purchasers' cost structures and eventual costs to wholesale customers who sell to consumers in other States. This relationship is a matter with respect to which Congress has given the Federal Power Commission paramount and exclusive authority. . . . The prospect of interference with the federal regulatory power in this area is made even more acute by the fact that criminal sanctions imposed by state statute for noncompliance fall upon such purchasers and not upon local producers.

Id. at 92.

The bases of the decision in *Northern Natural* could not have been more clear. The Kansas ratable take orders were thrown out because, (1) they were an attempt to directly regulate *purchasers* who were purchasing gas for transportation and resale in interstate commerce, and (2) the state's attempt to regulate *quantities* of gas purchased would inevitably conflict with and could seriously impair the Commission's "paramount and exclusive authority" to regulate the "intricate relationships between the purchaser's cost structures and eventual costs to wholesale customers who sell to consumers in other states." *Northern Natural*, 372 U.S. at 92. Thus, the conflict condemned in *Northern Natural* was not regulation of wellhead sales, but rather attempted regulation of the quantities of gas purchased by an interstate pipeline incident to its transportation and resale of that gas.

2. Serious supply imbalances between the intrastate and interstate markets, as well as concern about the overall level of price and supply of natural gas, led the Congress to enact the NGPA in 1978. The four major purposes of the NGPA have recently been characterized as follows:

> 1. To eliminate the disparity between interstate and intrastate markets.
>
> 2. Replace cost base regulation of wellhead prices with phased decontrol of most newly drilled gas.
>
> 3. Provide incentives to producers to engage in more exploration and production of natural gas while not permitting producers to reap windfall profits on gas discovered and produced for a relatively low cost.
>
> 4. Provide for an orderly transition to decontrol and mitigate the impact on residential consumers of the change in the way natural gas was controlled.

H.R. Rep. No. 814, 98th Cong., 2d Sess. 21 (1984). As this Court recently stated:

> The NGPA is designed to preserve the Commission's authority under the NGA to regulate natural gas sales from pipelines to their customers; however, it is designed to supplant the Commission's authority to establish rates for the wholesale market, the market consisting of so-called "first sales" of natural gas.

Public Service Commission v. Mid-Louisiana Gas Co., 103 S.Ct. 3024, 3031 (1983).

NGPA § 601[13] of the NGPA expresses how the NGPA has "supplanted" Commission regulation of first sales. Contrary to the opinion of the Mississippi Supreme Court, § 601(a)(1) does not purport to eliminate the Commission's jurisdiction over interstate pipeline companies. Commission jurisdiction over interstate pipelines does not attach *solely* because of a first sale.[14] Commission jurisdiction remains because interstate pipelines purchase all classifications of natural gas, transport it to other states, and resell the gas for ultimate public consumption.

3. The Commission claims its NGA jurisdiction includes control over the quantities and mix of *all* different categories of gas which a jurisdictional pipeline may purchase. *See FPC v. Louisiana Power & Light Co.*, 406 U.S. at 636. The Commission continues to assert jurisdiction over all of Transco's purchasing practices, despite price deregulation

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[13]15 U.S.C. § 3431.

[14]The key to understanding that § 601(a)(1) has not eliminated FERC's NGA jurisdiction over pipelines is the phrase "solely by reason of" found in § § 601(a)(1)(A), (B), and (D). § 601(a)(1) declared that the designated new types of natural gas listed therein would no longer be placed under the Natural Gas Act "solely by reason of" the fact that the "first sale" was in interstate commerce. Furthermore, under § 601(a)(1)(D), the producers would no longer be considered "natural gas companies" under the Natural Gas Act "solely by reason of" the fact that they sold this new gas in interstate commerce.

of some first sales under the NGPA. *See, e.g., Transcontinental Gas Pipe Line Corp.*, 23 FERC ¶ 61292 (1983); *Transcontinental Gas Pipe Line Corp.*, 14 FERC ¶ 61204 (1981).

The inevitable conflict between the Commission's asserted jurisdiction over interstate pipeline purchasing practices and state ratable take regulation is even more evident in light of the Commission's *Inquiry Into Purchasing Practices of Interstate Pipelines*, 48 Fed. Reg. 25264 (1983). There, in addition to denouncing the Mississippi Board's invasion of its jurisdiction, the Commission indicated it would determine what, if any, regulatory controls on the purchasing practices of pipelines under its jurisdiction are necessary or proper.

4. NGPA § 601 was not designed to and does not address the relationship between federal regulation and state regulation. However, § 602(a)[15] of the NGPA does deal with that relationship. Under § 602(a), Congress expressly stated that it was ceding to the states regulatory control only over "first sales" in the *intrastate* market. S. Conf. Rep. No. 1126, 95th Cong., 2d Sess. 124-5 (1978); *Exxon Corp. v. Eagerton*, 103 S.Ct. 2296, 2303 (1983). Further, states are limited to establishing their own maximum lawful prices for these intrastate transactions "in accordance with the overall national policy." *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 103 S.Ct. 697, 710 (1983); *Exxon Corp. v. Eagerton*, 103 S.Ct. at 2303.

When Congress wished to delegate its power to the states it did so expressly. Given the comprehensiveness of the NGPA, the failure to make such an express grant of authority for gas in interstate commerce is an implicit indica-

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[15] 15 U.S.C. § 3432.

tion by Congress that no such power was to be given to the states. *See Public Service Commission v. Mid-Louisiana Gas Co.*, 103 S.Ct. at 3034; *Botany Worsted Mills v. United States*, 278 U.S. 282, 289 (1928).

5. This Court has consistently held that Congress intended to completely occupy the field of natural gas sold and transported in interstate commerce. The pervasiveness of federal regulation of this field has heretofore precluded any state attempt to regulate natural gas sold or transported in interstate commerce. Since the enactment of the NGPA, this Court has, on two occasions, held that the federal domination of this field is still so complete that it precludes state regulation. *Exxon Corp. v. Eagerton*, 103 S.Ct. at 2304; *Maryland v. Louisiana*, 451 U.S. 725, 749-52 (1981) (citing *Northern Natural*). In neither of these cases was any direct conflict demonstrated between the state statutory scheme and existing FERC regulations. It was, rather, the mere infringement on the complete and exclusive federal regulatory scheme which preempted those state acts to the extent they applied to interstate pipelines or natural gas purchased and transported for resale in interstate commerce.

6. This Court has characterized the federal scheme of regulation as comprehensive even after the passage of the NGPA. Where Congress desired to allow some state regulation in intrastate sales of gas, it expressly delegated that power under § 602 of the NGPA. A substantial question is presented by this appeal as to (1) whether Congress has relinquished its complete occupation of the field of sales and transportation of natural gas in interstate commerce and (2) if so, whether Congress intended to give the states their first opportunity since 1938 to enter this field and regulate interstate pipelines.

II. Does the Enforcement of Mississippi's Regulations as to Purchases of High Cost Gas by Interstate Pipelines Impose an Undue Burden on Interstate Commerce?

There is currently a serious, nationwide problem in the natural gas industry. Despite a surplus of natural gas on the market, consumers and industries are forced to pay increasingly higher prices for this fuel as a result of federal regulation and the inflexibility of contracts between producers and pipeline purchasers of gas. *See* § 2, NATURAL GAS MARKET POLICY ACT OF 1984, H.R. 4277, 98th Cong. 2d Sess. (1984). Both Congress and the Department of Energy have recently devoted substantial attention to the causes and cures of this problem. *Id.*; EIA, *supra* note 3. This recent attention demonstrates a continuing federal interest in lower consumer gas prices.

This national problem can only be exacerbated by the action of the Board. The Board's recent enforcement of its Rule 48, combined with its refusal to consider the effect of its action on the interstate market, will inevitably cause increases in consumer prices of gas, and will have the practical effect of insulating Mississippi producers from a market problem common to producers in all states. Therefore, it violates the Commerce Clause of the United States Constitution. U. S. Const. art. I, § 8, cl. 3.

1. The present structure of the natural gas industry in this country is the product of many years of federal regulation under the Natural Gas Act and, more recently, the Natural Gas Policy Act of 1978. Between 1954 and 1978, the Commission regulated the price of gas in interstate commerce at the wellhead. However, in 1978 the NGPA was passed as a result of a shortage of gas available to the interstate market — a shortage caused principally by years of artifically low, controlled well-head prices. This shortage was characterized by inordinately high demand, a signifi-

cant reduction in exploration for new reserves and diversion of many available supplies of gas to the intrastate market. The NGPA extended federal control to the intrastate market to eliminate this disparity. It also allowed price increases with monthly escalations on all gas and price deregulation of "high cost" gas in order to encourage further development.

The NGPA goal of increased development was soon realized. After 1978, significant new reserves of natural gas were produced into the interstate market. By 1981, market demand began dropping. Factors such as conservation, reduction in the prices of competitive fuels, and unseasonably mild weather all contributed to this reduction in demand for natural gas. By 1982, deliverability to the interstate market exceeded demand. Broadman, *supra* note 3, at 9.

By 1982, interstate pipelines, which had faced severe shortages and the resulting curtailments before 1978, were faced with an oversupply of gas under burdensome contracts and a regulatory scheme designed to increase gas prices. Donald Hodel, the Secretary of Energy, succinctly described the problem in testimony before the House Energy Committee in 1983, stating:

> Pipelines are finding themselves bound by onerous contract terms they signed based upon a belief in scarcity that the regulations fostered. These contracts have prices tied to artificial regulatory ceilings that keep prices rising and they also have high take-or-pay provisions that incur the production of most expensive supplies first while production of less costly supplies is reduced . . . .

Proposed Changes to Natural Gas Laws (Part 1): Hearings Before the Subcomm. on Fossil and Synthetic Fuels of the House Comm. on Energy and Commerce, 98th Cong., 1st Sess. 293-94 (1983) (statement of Donald Hodel, U.S. Secre-

tary of Energy). The result was that consumer gas prices continued to increase despite an oversupply of gas on the market.[16]

In 1982, over 700 million dollars in take-or-pay costs were included in pipeline rates as a result of pipelines' inability to market contractually committed gas. EIA, *supra* note 3, at 38. Additionally, take-or-pay liabilities were expected to increase significantly in 1983 through 1985. *Id.* By 1982, the cost of gas purchased had become more than 70% of interstate pipelines' resale rates.[17] Finally, resale markets had become price sensitive due to the continued decrease in the prices of alternate energy sources, such as fuel oil. Broadman, *supra* note 3, at 9. The result was continued loss of industrial markets because of fuel switching, leaving the remaining consumers, primarily residential and commercial, to bear an even greater share of these increasing costs.

2. Despite the national market condition, the Board elected to enforce its Rule 48 against Transco. The effect of the Board's action, simply stated, was to require an interstate pipeline to take high cost gas it otherwise would not have to take. The Board expressly refused to consider evidence proffered on the interstate impact of such action and, at the same time, made no attempt to regulate the production in light of available market demand.

Transco had contracts with some, but not all, of the producers in the Harper Sand Gas Pool. However, it was ordered to take gas ratably from all producers in the pool. The Board left Transco with essentially three options to achieve ratable taking: (1) take no gas from these fields; (2)

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[16]By the end of 1982, consumer gas prices were up to 24% higher than a year earlier. Broadman, *supra* note 3, at 9.

[17]*See* Energy Information Administration, U. S. Department of Energy, *Natural Gas Monthly* 23, 29 (Aug. 1984).

further reduce contract purchases in the fields to accommodate the non-contract quantities of gas; or (3) reduce its contract purchases in other fields and states.

Since Transco was already taking less gas than the take-or-pay provisions of its gas purchase contracts specified, any option involved a reduction in contract purchases somewhere on Transco's system. *Any* reduction in contract purchases under (1), (2), or (3) above would add additional take-or-pay claims to the Transco system.

Rule 48 is not limited to the two fields involved in this specific case. The Board's regulation, if constitutional, can be expected to be enforced in every other price-deregulated field or pool in the state.[18] The impact of applying Rule 48 on a statewide basis is twofold. First, pipelines must take significant additional volumes of higher-priced deregulated gas from Mississippi—gas which they are not contractually obligated to purchase. To accommodate these additional volumes in a time of restricted market demand, the pipelines must either reduce purchases of lower cost regulated gas or reduce purchases of other deregulated gas under contracts which have take-or-pay provisions. Either option will result in an increase in gas prices.[19] Second,

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[18]The Mississippi Supreme Court made it clear it was sanctioning Board regulation of only gas deregulated under the NGPA. 467 So.2d at 1318 (App. A, *infra* at 29a).

[19]As noted in a recent study:

> The failure to take quantities of natural gas specified in supply contracts can subject pipelines to any of a variety of penalties. A survey of contract terms (EIA, 1982a) has shown that older contracts, involving gas with relatively low prices, are less stringent in their requirements or penalties than newer contracts for higher cost gas. As a result, when demand falls, pipelines may find it advantageous to reduce their purchases of old, low-priced gas. These purchase patterns can create an apparent supply glut,

because Mississippi is ignoring market demand in its regulation of production,[20] interstate pipelines will, as a practical matter, have to take more gas from Mississippi than they would otherwise. Therefore, they must necessarily purchase less gas from the producers in other states.

3. This Court has consistently instructed that one must look to the "practical effect" of any regulation in order to determine whether or not it imposes impermissible burdens on interstate commerce. *Lewis v. B. T. Investment Managers*, 447 U.S. 27, 37 (1980); *Hughes v. Oklahoma*, 441 U.S. 322, 336 (1979). However, the Mississippi Supreme Court dismissed the burden in this case by characterizing it as a burden solely on Transco rather than a burden on interstate commerce:

> It is hard to see how a ratable take rule or order could be said to generate an unreasonable burden on interstate commerce when the only thing requiring Transco (or any other interstate pipeline) to take at all, ratably or otherwise, is its own contract.

457 So.2d at 1322 (App. A, *infra* at 36a). This ignores the realities of the market-place. Long term contracts are at the heart of the interstate gas market. Purchased gas costs and

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> with some producers willing to sell more gas than is being taken at contracted prices. The pattern of gas production that results may also fail to meet given demand at minimum cost, as gas with higher production costs may be taken while that with lower production costs is shut in.

Broadman, *supra* note 3, at 10-11.

[20]Mississippi has a statutory policy against regulating production based on market demand except where necessary to prevent waste. Miss Code Ann. § 53-1-1 (1972).

the cost of take-or-pay payments are charged to the interstate consumer.[21]

The Commerce Clause is designed to protect the "natural functioning" of the interstate market from burdensome state regulation. *See Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 805-06 (1976). Take-or-pay provisions have been in interstate gas purchase contracts for many years.[22] Any Commerce Clause inquiry must therefore consider the existence of these provisions in determining the practical effect of state regulation.

4. This Court's analysis of Commerce Clause cases in recent years has been carried out under a balancing test which is enunciated in *Pike v. Bruce Church*, 397 U.S. 137 (1970). Under the *Pike* formula, one must not only weigh the benefits of a challenged state regulation against its interstate burden, one must also inquire into less burdensome regulatory alternatives which may be available to the state. Both the Board and the Mississippi Supreme Court refused to consider regulatory alternatives. The Mississippi

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[21]The Mississippi Supreme Court later recognized the true nature of the "practical effect" of this regulation by stating:

> Transco has the right to pass the costs it incurs in purchasing natural gas through to the consumer. 15 U.S.C. § 3431(c). In this sense, it is not Transco who experiences a burden, it is the consumer. If higher purchasing prices at the wellhead lead to higher prices to the consumer and a loss of markets, this is simply one inevitable consequence of the free market policies of the year of deregulation with respect to which Transco has vested by the negative commerce clause with no right to complain.

457 So.2d at 1322 (App. A *infra* at 37a-38a).

[22]In the 1963 *Northern Natural* case, the controversy was sparked by the impact of state ratable take regulations upon a pipeline with take-or-pay commitments in its contracts. 372 U.S. 89 and 372 U.S. at 98-99 (Harlan, J. dissenting).

Supreme Court sidestepped this admittedly serious inquiry by its finding that Transco had first failed to establish that the Board regulation poses an unreasonable burden on interstate commerce. 457 So.2d at 1322-23 (App. A, *infra* at 38a).

In this case, Mississippi has ignored a clearly constitutional alternative to achieve its stated purpose. The regulation of *production* of gas, rather than the interstate *purchasers*, would avoid forcing disproportionately high volumes of high cost gas onto the interstate market. This alternative means of preventing waste has been clearly sanctioned as constitutional. *Northern Natural*, 372 U.S. at 94 n.12; *Champlin Refining Co. v. Corporation Commission*, 286 U.S. 210, 235 (1932); *Colorado Interstate Gas Co. v. State Corporation Commission*, 386 P.2d 266, 285-86 (Kan. 1963), *cert. denied*, 379 U.S. 131 (1964).

The interstate pipelines should not be required to assume the burden of balancing production among wells. As stated in *Northern Natural*, such a "complex balancing task" is properly that of a state and should not be shifted to the shoulders of an interstate pipeline. 372 U.S. at 92.

5. The Commerce Clause question is substantial because the Board's action is discriminatory in effect. Mississippi has ignored regulatory alternatives which do not burden interstate commerce. The Board could have required producers to produce ratably only that quantity of gas which the market could take, and required that producers with contracts share the market. Instead the Board placed no restrictions on production and told Transco, which it knew had burdensome gas purchase contracts, to "ratably take and purchase high cost gas without discrimination."[23]

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[23]The Board stated that it was not concerned with Transco's problems or whether its markets could absorb the additional volumes of gas.

The result is production from Mississippi in excess of market demand. This is discriminatory in that it alters Mississippi's market share relative to other states. It is likewise discriminatory in that waste is avoided by burdening the consumer of an interstate commodity with price increases in a time of oversupply. A state may not legitimately protect the correlative rights of its citizens by placing itself in a position of economic isolation, ignoring problems common to all and forcing others to bear the burden of its regulations. *Philadelphia v. New Jersey*, 437 U.S. 617, 623, 627-29 (1978); *Pennsylvania v. West Virginia*, 262 U.S. 553, 596-600 (1923).

If Mississippi's approach is deemed constitutional, other states will surely follow its lead. The approach has political appeal because it prevents waste but it does not require the local producers to share the limited markets. It places the burden directly on the interstate market. Unfortunately, the ultimate impact will fall upon the consumer.

6. The Commerce Clause question in this case is also substantial because producers and the Mississippi Supreme Court have relied on the ruling in *Cities Service Gas Co. v. Peerless Oil & Gas Co.*, 340 U.S. 179 (1950), a decision later distinguished in *FPC v. Corporation Commission*, 362 F. Supp. 522 (W.D. Okla. 1973), *aff'd*, 415 U.S. 961 (1974).

In *Peerless*, Oklahoma found that an excessively low gas price promoted waste of natural gas. The state thus ordered a price increase from a range of 3.6 to 5 cents per thousand cubic feet up to 7 cents. This Court approved the regulations because they did not burden interstate commerce, stating: "[T]he wellhead price of gas is but a fraction of the price paid by domestic consumers at the burner-tip, so that the field

price as set herein may have little or no effect on the domestic delivered price."*Id.* at 187.[24]

In *FPC v. Corporation Commission*, a case affirmed by this Court, subsequent Oklahoma regulations which set a minimum price of 20 cents per thousand cubic feet were found to place an impermissible burden on interstate commerce. 362 F. Supp. at 535. The District Court found that "*Peerless* no longer controls insofar as it holds that minimum price orders are not within the proscription of the Commerce Clause." *Id.* One basis for distinguishing *Peerless* was the difference in amount of the minimum price orders and their impact on the ultimate consumer.[25] The three judge panel stated:

> The Court said in *Peerless*, that "the wellhead price of gas is but a fraction of the price paid by domestic consumers at the burner-tip, so that field price as herein set may have little or no effect on the domestic delivered price." In *Phillips* [*Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672 (1954)], however, the Court declared that the "rates charged may have a direct and substantial effect on the price paid by the ultimate consumers." And be it noted that Mr. Justice Clark, who spoke for the Court in *Peerless*, dissented in *Phillips*.

Id.

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[24]*Peerless* is distinguishable for additional reasons: there was no oversupply of gas on the market; the pipeline had no take-or-pay problems; the pipeline was also the major producer in the field; and, the court did not consider the availability of less burdensome alternatives.

[25]The other basis was lack of an expressed need for national uniformity at the time of *Peerless*. 362 F. Supp. at 535. Even in today's partially "deregulated" market, the need for a uniform national energy policy is still clear. *Energy Reserves*, 459 U.S. at 420-21.

In today's market, wellhead price is an even more important factor than at the time of *FPC v. Corporation Commission.*[26] The purchase cost of natural gas is now by far the largest component of the consumer price. In 1982, Transco's cost of gas was over 82% of the delivered price. The price increases which would be caused by Mississippi's regulation would have a substantial impact on the ultimate consumer and therefore demand a different ruling than that made in *Peerless.*

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[26]As noted in one study:

> The NGPA provides for certain types of expensive production to qualify for unregulated prices. This section 107 "high cost" or "deep" gas has been the subject of a great deal of controversy because some contracted prices reached a high of around $9.00/mcf in early 1982. The actual range of high-cost gas prices in mid-1982 was $3.15 to $9.65/mcf (EIA, 1982b). While only about 7 percent of all gas marketed in 1982 was deep gas, the large differential between these prices and those for other categories means that average pipeline acquisitions costs will be significantly influenced by high-cost gas purchase decisions.

Broadman, *supra* note 3, at 9-10.

CONCLUSION

Probable jurisdiction should be noted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, JEFFERSON D. STEWART, do hereby certify that I have caused to be mailed, postage prepaid, a true and correct copy of this Jurisdictional Statement to the following:

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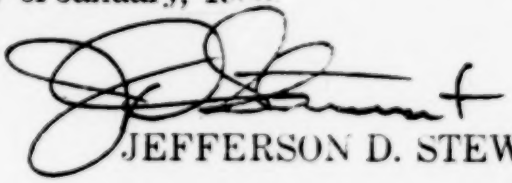
This the 2nd day of January, 1985



JEFFERSON D. STEWART

APPENDICES

APPENDIX A

IN THE SUPREME COURT OF MISSISSIPPI

No. 55,071

TRANSCONTINENTAL GAS PIPE LINE CORPORATION

v.

THE STATE OIL & GAS BOARD OF MISSISSIPPI AND COASTAL EXPLORATION, INC. *et al*

BEFORE ROY NOBLE LEE, P.J., ROBERTSON, AND SULLIVAN, JJ. ROBERTSON, JUSTICE, FOR THE COURT:

I. INTRODUCTION

This appeal arises out of a controversy regarding well head sales of natural gas produced in Marion County, Mississippi. This litigation has been conducted in the context of tensions created by collisions among basic principles of geology, economics and law when applied in a context where each litigant pursues self-interest.

The geological phenomenon of drainage necessitates, if considerations of fairness undergird our law, a rule that requires that a purchaser of natural gas (generally an interstate pipeline) take ratably from a common source of supply. That purchaser must market that gas, and the advent of deregulation has presented him with new and largely unanticipated difficulties in that regard. The natural gas market has become

glutted. Prices consumers are willing to pay have fallen sharply.

Overlaid upon these tensions are those inherent within our federal system. Until 1978 the federal sovereign indisputably had preempted all state regulation of wellhead sales of natural gas. Today we are presented a question of first impression: whether the Natural Gas Policy Act of 1978 (NGPA) 15 U.S.C. §§ 3301, et seq., continues in effect this federal preemption with respect to wellhead sales of *deregulated* natural gas. A complementary proposition suggests that the regulatory efforts of the State Oil and Gas Board constitute an impermissible burden on interstate commerce proscribed under long-established Commerce Clause jurisprudence.

Below we reject these and other claims advanced under federal law. We find, furthermore, that the State Oil and Gas Board has acted well within its statutory authority in requiring that an interstate pipeline take ratably (if it takes at all) the natural gas produced from a common source of supply.

The State Oil and Gas Board has acted beyond its authority, however, insofar as it has proscribed differentials in wellhead prices. No act of the Legislature of this state authorizes regulation or control of the price paid for natural gas at the wellhead. More specifically, no enactment of the Legislature vests in the State Oil and Gas Board any authority to regulate such prices.

Order No. 409-82 of the State Oil and Gas Board is affirmed in part and reversed in part.

II.

A. The Cast of Characters

The dominant characters, corporate all, before the Court today include:

Transcontinental Gas Pipe Line Corporation (Transco) is a Delaware corporation doing business in Mississippi. Transco is an interstate pipeline company which purchases natural gas from fields in Texas, Louisiana and Mississippi and the federal

off-shore domain. Transco transports this gas from these fields and sells it to customers along its pipeline which extends from southern Texas, through Mississippi, and up the east coast as far as New York. Transco was the principal Respondent before the Oil and Gas Board and is the Appellant here.

Coastal Exploration, Inc. (Coastal) is a Delaware corporation doing business in Mississippi. Coastal is a relatively small in-state oil and gas producer[1] and owns leasehold interests in gas-producing units in Mississippi. Coastal was the lead Petitioner below and is the lead Appellee here.

Tomlinson Interests, Inc. (Tomlinson) is a Texas corporation doing business in Mississippi. Tomlinson is an independent oil and gas producer which operates[2] one of the wells here involved. Tomlinson was one of two Respondents-turned-Petitioner below and is one of the Appellees here.

Getty Oil Company (Getty) is a Delaware corporation doing business in Mississippi. Getty is an oil and gas producer which operates three of the wells here involved. Getty was the other

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[1]The term "producer" as used in this opinion means the owner of all or part interest in a well or wells capable of producing natural gas. An "owner" may also be a "producer" Miss. Code Ann. § 53-1-3(h) (Supp. 1983); Statewide Rule 2(g), Miss. Oil and Gas Board Rules, promulgated November 19, 1951, effective January 1, 1952.

> The term "Owner" has been defined as any
>
> person who has the right to drill into and produce from any pool, and to appropriate the production either for himself or for himself and another or others. . . .

Miss. Code Ann. § 53-1-3(g) (Supp. 1983); Statewide Rule 2(p), Miss. Oil and Gas Board Rules, promulgated November 19, 1951, effective January 1, 1952.

[2]The term "operator" as used in this opinion means

> any person who, duly authorized, is in charge of the development of a lease or the operation of a producing well.

Statewide Rule 2(r), Miss. Oil and Gas Board Rules, promulgated November 19, 1951, effective January 1, 1952. An "operator" may also be a "producer" or an "owner" or both.

Respondent-turned-Petitioner below and is one of the Appellees here.

Supporting actors, all Petitioners before the Board, include:

Wiley Fairchild and Rodney Fairchild (Fairchilds) are adult resident citizens of Forrest County, Mississippi, each of whom owns an individual working interest in one of the wells here involved.

W. R. Fairchild Construction Company, Ltd. (Fairchilds) is a Mississippi corporation domiciled in Forrest County, Mississippi, and owns an undivided working interest in one of the wells here involved.

Susan W. Clements Lay (Lay) is an adult resident citizen of Hinds County, Mississippi, who owns an undivided working interest in one of the wells here involved.

Lane Petroleum Corporation (Lane) is a Mississippi corporation which owns an undivided working interest in one of the wells here involved.

Louis E. Ridgway, Jr., (Ridgway) is an adult resident citizen of Hinds County, Mississippi, who owns an undivided working interest in one of the wells here involved.

Daniel E. Herlihy (Herlihy) is an adult resident citizen of Hinds County, Mississippi, who owns an undivided working interest in one of the wells here involved.

Bryant M. Allen (Allen) is an adult resident citizen of Hinds County, Mississippi, who owns an undivided working interest in one of the wells here involved.

Inexco Oil Company (Inexco) is a Delaware corporation doing business in Mississippi. Inexco is a small interest owner in four wells here involved.

Of these supporting characters, only the Fairchilds and Inexco took any part in the formal hearing held by the State Oil

and Gas Board, and only Inexco has entered its appearance and filed a brief before this Court. The others are listed because each filed with the Board an informal complaint charging Transco with failure to take ratably.

The State Oil and Gas Board (the Board) is a party to this appeal. The Board is an administrative agency of the State of Mississippi created by virtue of Chapter 256, Miss. Laws of 1948, now codified as Miss. Code Ann. § 53-1-5 (Supp. 1983), authorized in relevant part to make and enforce reasonable rules, regulations and orders protecting against abuse of the correlative rights and opportunities of each owner of oil or gas in a common source of supply and charged with the conduct of hearings such as that held September 14-16, 1982, which has generated Order No. 409-82, the Circuit Court's affirmance of which is here under attack. The Board is an Appellee here.

B. The Drainage Phenomenon

At the core of this case is the geological phenomenon of drainage. That phenomenon has been described by this Court in *Shell Oil Company v. James*, 257 So.2d 488 (Miss. 1972).

> When the pool of oil has been penetrated by a recovery well the oil and gas located in the pool move from a high pressure area to a low pressure area so that the oil and gas migrate from the property of one landowner to another. This exodus is called drainage. 257 So.2d at 494-495.

The phenomenon has been similarly described by the Supreme Court of Kansas in *Northern Natural Gas Company v. State Corporation Commission*, 188 Kan. 355, 362 P.2d 599 (1961):

> While the members of this court make no claim to be experts in the science of the production of natural gas, we believe that the court may take judicial notice of the fact that where natural gas is within the earth in one common source and is under pressure, if one gas well is allowed to take gas, this will result in the pressure being lowered around the vicinity of this gas well so that the gas in the

> common source will tend to drain or rush to the vicinity of the well taking gas. The result will be that the other wells in the common field or source will be able to produce much less gas and the owners of such wells will have suffered a definite loss. 188 Kan. at 358, 362 P.2d at 602

In recognition of the relatively helpless position of the party whose gas is being drained, our law has moved to ameliorate the injustice produced by drainage. Such is the genesis of Statewide Rule 48 promulgated by the State Oil and Gas Board over 30 years ago on November 19, 1951. That rule provides

> RULE 48. Ratable Take.
>
> Each person now or hereafter engaged in the business of purchasing oil or gas from owners, operators, or producers shall purchase without discrimination in favor of one owner, operator, or producer against another in the same common source of supply.

Questions regarding the meaning, validity and enforceability of Rule 48 are at the center of this case.

Drainage has spawned much litigation in this state. All prior litigation appears to have arisen in the context of one owner of an undivided interest suing another such owner with the plaintiff claiming that the defendant was taking, i.e., draining, the plaintiff's gas. *Shell Oil Company v. James*, 257 So.2d 488, 490 (Miss. 1971); *see generally*, Comment, *Implied Covenant To Protect Leased Premises From Drainage, Etc.*, 35 Miss. L.J. 280, 280-95 (1964) (basis for suits between individuals); Kuntz, *Correlative Rights In Oil and Gas*, 30 Miss. L.J. 1, 1-9 (1958) (same). Insofar as we can ascertain, this is the first time a court of this state has been called upon to consider Rule 48 or in any other context to grant relief against a purchaser of natural gas for drainage loss. *See In Re Petition of Cenard Oil and Gas Co.*, Docket No. 60-64-92, Order No. 81-64, dated April 16, 1964, (Board cited Southern Natural Gas Co. for refusal to take ratably from owners of all interests in common source of sup-

ply; apparently order was not appealed). In this and other contexts, this action plows new furrows.

C. The Background Facts

Greens Creek Field and East Morgantown Field are two natural gas "fields"[3] located in Marion County, Mississippi. Greens Creek Field was discovered by the Harkins and Company—Board of Supervisors Well in 1976. The Harper Sand Gas Pool[4] of that field was first encountered by the Tomlinson Interests, Inc.—J. C. Williamson Well in 1978. Approximately 5 miles south of the J. C. Williamson Well, Tomlinson Interests, Inc. discovered East Morgantown Field, and its Harper Sand Gas Pool, with its Board of Education Well in March, 1979.[5]

These two fields had been defined as separate fields by the Board by late 1980. In 1980, Getty Oil Company discovered

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[3]The term "field" has been defined in our law as

> the general area which is underlaid or appears to be underlaid by at least one pool; and "field" shall include the underground reservoir or reservoirs containing oil or gas or both. The words "field" and "pool" mean the same thing when only one underground reservoir is involved; however, "field", unlike "pool", may relate to two or more pools.

Miss. Code Ann. § 53-1-3(f) (Supp. 1983); Statewide Rule 2(o), Miss. Oil and Gas Board Rules, promulgated November 19, 1951, effective January 1, 1952.

[4]The term "pool" has been defined in our law as

> an underground reservoir containing a common accumulation of oil or gas or both. Each zone of a general structure which is completely separated from any other zone in the structure is included in the term "pool" as used herein.

Miss. Code Ann. § 53-1-3(e) (Supp. 1983); Statewide Rule 2(n), Miss. Oil and Gas Board Rules, Promulgated November 19, 1951, effective January 1, 1952. The term "pool" is synonymous with "common pool or source of supply" in the Conservation Act's declaration of policy, Miss. Code Ann. § 53-1-1 (Supp. 1983) and with the phrase "same common source of supply" as used in Statewide Rule 48, Miss. Oil and Gas Board Rules.

[5]Reservoir discovery data taken from the Mississippi State Oil and Gas Board Mississsippi Oil and Gas Production Reports for 1978, 1979 and 1980.

additional Harper Sand production directly between these two fields with its Rogers 28-11 Well No. 1.

We now know that the The Harper Sand Gas Pool underlies portions of both the Greens Creek Field and the East Morgantown Field. The two fields are contiguous. If only one well were completed into this pool and natural gas were produced from the pool via that one well, the entire pool would eventually be drained.

At the time of the Board hearing in mid-September, 1982, there were at least six gas wells which had been completed into and which were producing from the Harper Sand Gas Pool: The Getty-Rogers 28-11 Well, the Getty-Sipp 20-9 Well, the Getty-Buckley 33-6 Well (all three operated by Getty), the Tomlinson-Willoughby 3-5 Well (operated by Tomlinson), and the Florida Exploration--Carlisle 4-2 Well and the Florida Exploration-Barnes 29-1 Well (both operated by Florida Exploration Company).

The Harper Sand Gas Pool produced by these wells lies below 15,000 feet. All of the wells producing from this pool have been classified as "deep, high-cost wells" under Section 107(c)(1) of the Natural Gas Policy Act of 1978 (NGPA); 15 U.S.C. § 3317(c)(1).

In 1978, Transco began contracting with producers in Greens Creek Field and, on the basis of those reserves thereby committed, extended its pipeline facilities to that field. When East Morgantown Field was discovered, Transco also began entering into contracts with producers and, as a result thereof, extended its pipeline facilities to those wells to recover the dedicated reserves. Transco entered into additional contracts with producers in 1980 to cover their production where the fields merged.

At the beginning of 1982, Transco had approximately thirty-five different contracts with various owners and producers in these two fields, including Getty and Tomlinson. These contracts had been made at various times between 1978 and 1982

and, because of different market conditions, had substantially different terms and conditions. Prior to July 1, 1982, Transco had not placed any restrictions on the contract owners and producers as to how much gas Transco would take under these contracts.

Coastal owns small undivided working interests (generally less than 1%) in the units of four of the wells which produce from this pool. These are the Rogers, Sipp, Willoughby and Barnes wells. Coastal participated in the drilling of each of these wells, paid its share of drilling and completion costs, and has paid its share of operating costs for each of these wells.

On August 6, 1980, Getty, as the operator and owner of a substantial working interest in the Getty-operated units, entered into a gas purchase contract with Transco. Among the terms of that contract was a price at the wellhead of § 7.907 per one million British thermal units (mmbtu) of gas. When the wells in question first began producing gas in April 1981, beginning with production from the Sipp Well, the gas was sold to Transco.

Many owners (including Coastal) of small undivided interest in the Getty-operated wells had no gas purchase contract when first production began. However, Getty produced all owners' gas and delivered the gas to Transco which in turn purchased and paid for all gas at the same price and on the same terms and conditions as Transco purchased and paid Getty for its gas.

As the other wells completed into the pool began producing, the same procedure was followed, with the effect being that Transco took gas ratably as between the wells producing from the pool.

At the outset of the year 1982, Transco held contracts for the purchase of natural gas from these six wells at prices ranging from a low of $5.00 per mmbtu to a high of $9.054. A representative sampling of those contracts includes:

Contract Number	Date	Seller(s)	Price
06646	09/05/78	Tomlinson Interest, Inc.	6.511 + tax
06690	12/12/78	Harkins & Company	9.054 + tax
06695	12/12/78	First Energy Corporation	"
06696	12/12/78	St. Joe Petroleum (U.S.)	"
06707	12/12/78	Amerada Hess Corporation	"
06991	08/06/80	Getty Oil Company	7.907 + tax
61008	08/22/80	Florida Exploration Company	8.4066 + tax
61045	08/22/80	ACF Petroleum Company	"
61039	11/26/80	Southland Royalty Company	8.065 + tax
61084	03/09/81	Jones O'Brien, Incorporated	8.161 + tax
61218	12/01/81	Sabine Production Company	5.00
61220	01/01/82	Sabine Production Company	5.00

In the spring of 1982, Transco began to experience problems in reselling the gas on its system. As the result of escalating gas costs and declining prices of competing fuel oil, end-use industrial customers of distribution companies served by transco were switching from gas to cheaper fuel oils. By May of 1982, Transco had lost resale markets for approximately 95-100 million cubic feet of gas per day. Because the costs of gas were continuing to rise, Transco projected an additional $.65-$.70 per mmbtu increase in its average cost of gas and thus the inevitable loss of additional markets. Because it was experiencing market loss at its distribution end and was projecting further losses, Transco invoked the "market-out" provisions in all contracts

containing those provisions and began paying those sellers $5.00 per mmbtu.

Coastal Exploration, Inc. had no contract with Transco. Coastal had elected to allow Getty, Florida Exploration, and Tomlinson, the operators of the wells in which it had an interest, to sell its share of gas "under the operating agreement."[6]

In May of 1982, Transco notified Getty and Tomlinson that effective June 1, 1982 (later changed to July 1, 1982), Transco would no longer take or purchase the gas of the "non-contract producers", those owners and producers who had not entered into a gas purchase contract with Transco. However, because of certain provisions of the Florida-Transco gas contract, Transco would continue to purchase non-contract producers' gas produced from the Florida--

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[6]An operating agreement is the usual means in the oil and gas industry of defining the rights and duties of an operator *vis a vis* the non-operating owners of a well. In this case, every well involved in this dispute was covered by a form operating agreement known as the AAPL Form 610-1977 Model Form Operating Agreement. Of particular interest is the provision in that agreement concerning the sale of gas owned by non-operators:

> Each party shall take in kind or separately dispose of its proportionate share of all oil and gas produced from the contract area, exclusive of production which may be used in development and producing operations and in preparing and treating oil and gas for marketing purposes and production unavoidably lost . . ..
>
> In the event any party shall fail to make the arrangements necessary to take in kind or separately dispose of its proportionate share of the oil and gas produced from the contract area, operator shall have the right, subject to the revocation at will by the party owning it, but no the obligation, to purchase such oil and gas or sell it to others at any time and from time to time, for the account of the non-taking party at the best price attainable in the area for such production. . . . *Any purchase or sale by operator of any other party's share of oil and gas shall be only for such reasonable periods of time as are consistent with the minimum needs of the industry under the particular circumstances but in no event for a period of in excess of one year.* [emphasis added]

operated wells and pay those producers the same price Transco paid Florida.

After receiving this notice from Transco, Getty and Tomlinson notified Coastal that they, as operators, would not produce Coastal's share of gas from the Rogers, Sipp and Willoughby Wells unless Coastal obtained its own gas purchase contract. A similar type notice was sent to other non-contract producers and owners.

Following the notice from Getty and Tomlinson, Coastal attempted to secure another purchaser to whom it could sell its gas but was unsuccessful. In June of 1982, Coastal asked Transco to be allowed to ratify Getty's 1980 contract. Transco refused, unless Coastal would agree to amend the price to $5.00/mmbtu, to add a "market-out clause" (a clause which would allow Transco to adjust the purchase price if the contract price became "uneconomic"), and to nominate a seller's representative. Coastal rejected this offer, at which time Transco refused to take Coastal's gas at all. Coastal then filed its Petition asking the Board to require Transco to purchase its share of gas from the Getty operated wells under the same terms and conditions Transco was purchasing Getty's gas.

Transco did not want or need any more high cost gas because of its market situation. However, in July and August of 1982, it submitted the same offer that it had already made to Tomlinson and Coastal to all non-signatory producers and owners it knew about in Getty and Tomlinson operated wells. The only difference between the 1980 Getty contract and Transco's offer was the pricing provisions and the requirement that they nominate a single seller's representative for each well. At the time of the Board hearing, 55 non-signatory producers and owners in these wells had accepted Transco's offer.

The then-current market value of high cost gas in East Morgantown or Greens Creek Field was no more than what

Transco had offered to the non-signatory producers and owners and was currently paying under its "market out" contracts, *i.e.*, $5.00/mmbtu.[7]

Effective July 1, 1982, as to the Getty-Sipp and Rogers Wells, and effective August 19, 1982, as to the Tomlinson-Willoughby Well, Transco ceased to take gas attributable to the interests of any non-signatory producer or owner in the wells until and unless that producer or owner accepted Transco's $5.00 offer. As a result, Transco's takes of gas and the rates of production from the common pool by these wells were "cut back" to below the maximum efficient rate of flow of the wells.[8] Thereafter, for all practical purposes, the wells produced only and Transco purchased only a rate of production equal to the operators' and other signatory producers' and owners' interests in the maximum efficient rate of flow from the wells.

The situation at the Florida-Carlisle and Barnes Wells, was different, and significantly so. Transco continued to purchase the non-signatory producers' and owners' gas which was produced from these two wells and tendered to Transco by Florida, the operator, on the same terms and conditions and at the same price which Transco paid for Florida's gas. Thus, while the Sipp, Rogers and Willoughby Wells were cut-back to below their respective allowables

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[7]For a perceptive consideration of the natural gas market today, see Pierce, *Reconsidering The Roles of Regulation And Competition In The Natural Gas Industry*, 97 Harv.L.Rev. 345 (1983); and Pierce, *Natural Gas Regulation, Deregulation and Contracts*, 68, Va.L.Rev. 63 (1982). In the former article, Prof. Pierce documents the statement that "the market for gas would clear today at a price somewhere between four and five dollars". 97 Harv.L.Rev. at 351 (see note 43 and accompanying text).

[8]The Mississippi State Oil and Gas Board determines the maximum *allowable* natural gas withdrawal rates for each gas producing pool. Each well's *allowable* is its "maximum efficient rate of production" as determined by semi-annual deliverability tests made by the operator of each well. See Rule 34(B), Miss. Oil and Gas Board Rules, promulgated November 19, 1951, effective January 1, 1952.

because of Transco's refusal to take and purchase gas, the Barnes and Carlisle Wells continued to be produced at their respective allowables because of Transco's takes and purchases of gas from those wells.

The result of Transco's actions has been and, if allowed to continue, will be non-uniform, disproportionate and unratable withdrawals of gas from the common pool causing undue drainage between tracts of land, that is, drainage and undue drainage *from* the Getty and Tomlinson operated units *to* the Florida operated units producing from the common pool. The result of Transco's actions has also been and, if allowed to continue, will be one or more owners in the common pool producing more than their just and equitable share of the production from the pool.

There is a second form of loss to which the nonsignatory producers and owners will be potentially subject as a result of Transco's actions. If Transco continues to take only the gas it is contractually obligated to take, the remaining gas, though still in the pool, will be much more difficult to retrieve. This is because the pressure in the pool will lower as gas is produced. In this way contracting owners such as Getty will be able to produce more than their just and equitable share of the production from the pool, absent, of course, enforcement of a requirement that contracting owners produce all owners' gas ratably.

It should be noted that Transco was not the only pipeline purchasing gas produced by these wells. Tennessee Gas Pipe Line Co. was also a market outlet for the various owners. The relative percentages in each well under contract first to Transco, then to Tennessee, as well as the interests not under contract are shown on the following table.

Percentage Gas Represented To Be Dedicated Under Gas Purchase Contract

	Transco	Tennessee	WI Owners Who Refused to Sell To Transco & Who Are Still Uncommitted	Balance
Rogers 28-11 (Getty)	45.27489% (14)	2.35040% (8)	33.65260% (2)	18.72211%
Sipp 20-9 (Getty)	70.28732% (33)	9.38427% (17)	11.54930% (1)	8.77911%
Willoughby 3-5 (Tomlinson)	53.14003% (11)	3.40061% (6)	25.66083% (11)	17.79853%
Buckley 33-6 (Getty)	79.95812% (6)	11.34146% (3)	-0- (0)	8.70042%
Carlisle 4-2 (Florida)	63.30590% (4)	29.61460% (9)	1.56250% (1)	5.51700%
Barnes 29-1 (Florida)	65.14900% (4)	11.61600% (11)	-0- (0)	23.23500%

As of the Board hearing in mid-September of 1982, Tennessee was not taking any gas from these six wells. Tennessee had also refused to purchase Coastal's gas. Apparently, Tennessee viewed its market position as Transco did its.

B. Proceedings Below

On July 29, 1982, Coastal commenced these proceedings by filing its petition with the State Oil & Gas Board. Coastal asked

that Transco be required to comply with Statewide Rule 48 by ratably taking gas from the wells producing from the common pool and purchasing without discrimination in favor of the operators, Getty and Tomlinson, against Coastal.

The Fairchilds, owners in the Rogers 28-11 Well, joined in the Petition.

At the hearing before the Board in mid-September 1982, Transco claimed that Statewide Rule 48 was invalid as a matter of state law and that Board had no authority to require Transco to ratably take or purchase without discrimination. Transco argued that federal law had preempted the area and that Rule 48 was unconstitutional for a variety of reasons.

A three day trial was held before the Board during which Transco defended the action by the presentation of witnesses, exhibits and legal arguments, raising as defenses the same claims which it is now asserting before this Court.

On October 13, 1982, the Board ruled in favor of the producers and by its Order No. 409-82 directed Transco to,

> comply with Statewide Rule 48 of the State Oil and Gas Board of Mississippi in its purchases of gas from the East Harper Sand Gas Pool in Greens Creek and East Morgantown Fields and . . . ratably take and purchase gas without discrimination in favor of one owner, operator or producer against another in the said common source of [sic] pool; and, specifically, in the event it so chooses and elects to take and purchase gas from said common pool, Transco shall ratably take and purchase without discrimination in favor of the operators, Getty and Tomlinson against Coastal, the Fairchilds, and Inexco.

Transco, employing Miss. Code Ann. § 53-1-39 (Supp. 1983), appealed to the Circuit Court of the First Judicial District of Hinds County, Mississippi, which on June 28, 1983, released a thorough and competent opinion affirming Order No. 409–82 in its entirety. This appeal has followed. *See* Miss. Code Ann. § 53-1-45 (Supp. 1983).

C. The "Non-Facts"

Before considering the various questions tendered on this appeal, three red herrings need to be disposed of. The facts of this case have been argued as vigorously as the law. Perhaps because much is at stake the parties with more than occasional frequency have reminded us of facts which are of *no* legal significance. These "non-facts" are identified here.

First, nothing here turns on size. That Transco and Getty may be large corporations and that Coastal may be a small corporation simply does not matter. The size of the interest of a party in the various wells is likewise irrelevant. Each party before this Court today stands equal to each other in justice-worthiness.

Second, nothing turns on the domicile of the parties. That some are Mississippians and some are not is of no significance. Today we apply controlling principles of law to relevant facts—and whether a party is Mississippi-based is not among those relevant facts.

Third, the economic consequence of today's decision for one or more of the parties is of no significance, except insofar as the law has provided otherwise. For example, drainage is of serious economic consequence if it occurs and applicable rules of law have given some of these parties protections from it. On the other hand, we have given no thought to whether Transco can sell all the gas it is lawfully required to take, only to the articulation of how much gas Transco is lawfully required to take. Similarly, we have no concern that some non-contract interest owners in the wells in issue may not obtain the return on investment they once expected.

Holmes put the point well in *The Path of The Law*, 10 Harv. L. Rev. 457 (1897)

> The reason why a lawyer does not mention that his client wore a white hat when he made a contract, while Mrs. Quickly would be sure to dwell upon it along with parcel gilt goblet and the sea-coal fire, is that he forsees that the

> public force will act in the same way whatever his client had upon his head. 10 Harv. L. Rev. at 458.

As former lawyers not wanting to appear as Mrs. Quicklys, we advise one and all that the size of the parties and their interests, their states of domicile, and the economic consequences to them of today's decision are of no relevance to our determination how the public force ought act on them.

III. SCOPE OF JUDICIAL REVIEW

We note at the outset the well-settled scope of judicial review of an order of the Oil & Gas Board. The question before the reviewing court is

> whether the order is supported by substantial evidence, is arbitrary or capricious, beyond the power of the Board to make, or violates some constitutional right of the complaining party.

California Co. v. State Oil & Gas Board, 200 Miss. 824, 842, 27 So.2d 542, 546 (1946); *Damson Oil Corp. v. Southeastern Oil Co.*, 370 So.2d 225, 229 (Miss. 1979) (quoting *California Co.*); *Masonite Corp. v. State Oil & Gas Board*, 240 So.2d 446, 448 (Miss. 1970) (same); *Superior Oil Co. v. State Oil & Gas Board*, 220 So.2d 602, 603 (Miss. 1969) (same).

The findings of an administrative agency like the Board are prima facie correct and the reviewing court may not substitute its judgment for that of the administrative agency where there is a substantial basis in the evidence for those findings. *Barnwell, Inc. v. Sun Oil Co.*, 249 Miss. 398, 410-11, 162 So.2d 635, 640 (1964); *State Oil & Gas Board of Mississippi v. Brinkley*, 329 So.2d 512, 515-516 (Miss. 1976); *Masonite Corp. v. State Oil and Gas Board*, 240 So.2d 446, 448 (Miss. 1970); *Damson Oil Corp. v. Southeastern Oil Co.*, 370 So.2d 225, 229 (Miss. 1979).

Well within our authority is a plenary consideration of the claims tendered by Transco based in federal constitutional law, to wit: the claims that Rule 48 and Order No. 409-82 contravene

the Supremacy Clause, the Commerce Clause and the Due Process Clause of the United States Constitution.

Also well within our review authority is a consideration of the question whether Rule 48 or Order No. 409-82, or any part of either, transcends the authority vested by the Mississippi Legislature in the State Oil and Gas Board and is thus beyond the lawful power of the Board to make. Where we find such a transcension, it becomes our responsibility and obligation to declare the offensive portion of the rule or order invalid and unenforceable.

IV. TRANSCO'S CLAIMS UNDER FEDERAL LAW

A. Federal Preemption

The initial thrust of Transco's appeal is that this state's authority to make and enforce a law such as Rule 48 has been effectively preempted by the United States. In Assignment of Error No. 3, Transco says that this preemption has occurred by virtue of the so-called negative Commerce Clause, that long established construction of the Commerce Clause of the Constitution of the United States which limits the authority of the states to enforce unreasonable burdens on interstate commerce. Complementing that argument is the one we consider now, made under Assignment of Error No. 2, to the effect that the Congress, in the exercise of its powers affirmatively granted under the Commerce Clause, has preempted state regulation by virtue of the Natural Gas Act, 15 U.S.C. §§ 717-717w, and the Natural Gas Policy Act of 1978, Pub.L.No. 95-621, 92 Stat. 3352 (1978), codified at 15 U.S.C. §§ 3301 et seq., and the authority and responsibilities vested thereby in the Federal Energy Regulatory Commission (FERC).

The Supremacy Clause of the Constitution of the United States provides that all valid enactments of the Congress shall be the supreme law of the land

> and the Judges of every state shall be bound thereby, anything in the Constitution or Laws of any State to the contrary notwithstanding. U.S. Const. art. VI, § 2.

From this source has sprung the doctrine of federal preemption of state law. Federal law has preemptive effective when the Congress acting within its constitutional powers expressly so provides. *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, ____ U.S. ____, 103 S.Ct. 1905, 1912, 76 L.Ed.2d 1, 13-16 (1983); *Fidelity Federal Savings and Loan Association. v. De La Cuesta*, 458 U.S. 141, 152-53, 102 S.Ct. 3014, 3022-23, 73 L.Ed.2d 664, 674-75 (1982); *Jones v. Rath Packing Co.*, 430 U.S. 519, 525-526, 97 S.Ct. 1305, 1309-1310, 51 L.Ed.2d 604, 613–14 (1977). This Court has respected the preemptive effect of such enactments. *See, e.g., International Association of Bridge, Structural & Ornamental Ironworkers, AFL-CIO Local Union No. 710 vs. Howard L. Byrd Building Service, Inc.*, 284 So.2d 301, 302-303 (Miss. 1973) (federal labor law preempts); *Hattiesburg Building & Construction Trades Council v. Mississippi Mechanical Contractors, Inc.*, 207 So.2d 99, 102-103 (Miss. 1968) (same).

It is now well recognized that state law may be preempted even in the absence of an express congressional enactment to that effect. This view has recently been articulated in *Pacific Gas & Electric Co. v. State Energy Resources Conservation & Development Commission*, ____ U.S. ____, 103 S.Ct. 1713, 75 L.Ed.2d 752 (1983), as follows:

> "Absent explicit preemptive language, Congress' intent to supersede state law altogether may be found from a 'scheme of federal regulation so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it,' 'because the Act of Congress may touch a field in which the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject,' or 'because the object sought to be obtained by federal law and the character of obligations imposed by it may reveal the

> same purpose.' [Citations omitted] Even where Congress has not entirely displaced state regulation in a specific area, state law is preempted to the extent that it actually conflicts with federal law. Such a conflict arises when 'compliance with both federal and state regulations is a physical impossibility,' [Citations omitted] or where state law 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'
>
> —103 S.Ct. at 1722, 75 L.Ed.2d at 765; *Exxon Corp. v. Eagerton*, ____ U.S. ____, 103 S.Ct. 2296, 2301, 76 L.Ed.2d 497, 505 (1983); *see Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, ____ U.S. ____, 103 S.Ct. 1905, 1912, 76 L.Ed.2d 1, 14-16 (1983) (decision not to regulate can be as preemptive as one to regulate).

The State Oil and Gas Board has attempted to achieve equity and protect owners in a common pool from loss through drainage by the promulgation and enforcement of a rule requiring purchasers at the wellhead to take ratably. Transco, however, argues that Rule 48 as construed and interpreted in Order No. 409-82 regulates an aspect of natural gas production exclusive regulatory jurisdiction over which has been vested by the Congress in FERC. State power, accordingly, has been preempted and, Transco argues, the Circuit Court erred in failing to so hold.

We consider Transco's affirmative preemption claim against the backdrop of our confidence that the State of Mississippi has the authority to regulate the production of natural gas from pools or fields situated within this state. *Superior Oil Co. v. Foote*, 214 Miss. 857, 874-878, 59 So.2d 85, 92-94 (1952). After all, such production is essentially an intra-state (intra-Mississippi) activity. This authority has, generally speaking, been delegated to the State Oil and Gas Board, and constitutionally so. *Barnwell, Inc. v. Sun Oil Co.*, 249 Miss. 398, 406, 162 So.2d 635, 638 (1964). We are concerned here with an authority this state has lest it be preempted by paramount authority emanat-

ing from another sovereign, the United States of America. *Cities Service Gas Company v. Peerless Oil and Gas Company*, 340 U.S. 179, 186-87, 71 S.Ct. 215, 219-20, 95 L.Ed. 190, 202 (1950).

All parties agree that prior to 1978 there existed in the Federal Energy Regulatory Commission (formerly the Federal Power Commission) plenary authority to regulate the sale and transportation of natural gas in interstate commerce. No one questions that prior to 1978 this federal authority within its sphere was more than sufficient to preempt any otherwise lawful state authority. *Northern Natural Gas Co. v. State Corporation Commission of Kansas*, 372 U.S. 84, 89-90, 83 S.Ct. 646, 649, 9 L.Ed.2d 601, 606 (1963). Prior to 1978 this state was without authority to enforce Rule 48 requiring ratable taking, and any order such as Order No. 409-82 would have been wholly *ultra vires*.

In 1978 the Congress enacted and the President signed into law the Natural Gas Policy Act of 1978 (NGPA). 15 U.S.C. §§ 3301, et seq. Transco emphasizes that by virtue of this enactment the Congress extended federal regulation to intrastate gas. This was done to eliminate price discrepancies then existing between intrastate and interstate markets which were encouraging producers to withhold new supplies of gas from the heavily regulated interstate market.

Coastal and the other producers, on the other hand, remind us that the Congress also coupled with that extension of regulation a comprehensive plan of deregulation under which some gas was immediately deregulated, other gas was more gradually deregulated, and regulated gas prices were allowed to escalate, all in order to provide producers, operators and pipeline purchasers with the degree of freedom from regulation and the price incentives necessary to encourage discovery and production of more gas and thus alleviate the theretofore

seemingly perpetual natural gas shortage.[9] We are here concerned only with *deregulated* natural gas.

The Congress specifically found that, under the old Natural Gas Act, FERC (formerly FPC) had kept "just and reason-

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[9]Prof. Richard J. Pierce, Jr., has described well the basic statutory scheme of the Natural Gas Policy Act of 1978.

> For purposes of deregulation, the NGPA can be considered to have created three major categories of gas. *"High-cost gas," a narrowly defined category that accounts for only a tiny fraction of aggregate gas supply, was deregulated in November 1979.* "New gas," the second category, was subject to price ceilings for various subcategories that resulted in an average price of $2.42 per MMBtu in 1980. These ceilings will increase over time in constant dollars, because most new gas price ceilings will increase at a rate slightly higher than inflation. New gas will be deregulated sometime between 1985 and 1988. "Old gas," the third category, is subject to price ceilings for various subcategories that result in an average price of approximately $1.75 per MMBtu. With the exception of some intrastate old gas that will be deregulated in 1985, old gas will continue to be subject to the same price ceilings in constant dollars indefinitely, because the price ceilings applicable to most subcategories of old gas will increase over time only at the inflation rate.
>
> Under the NGPA, Congress expected deregulation to occur gradually through the following sequence. *First, high cost gas was deregulated in 1979 in recognition of the need for special economic incentives to encourage exploration for and production of high cost gas.* Second, new gas and most intrastate gas is scheduled for deregulation between 1985 and 1988 as the major step in the deregulation process. The annual increase in the price ceiling for new gas was expected to ease the transition to deregulation by permitting the price of new gas to reach approximate parity with the market price of oil by the time of deregulation. Third, although old gas is never scheduled for deregulation, the gas production market is expected to evolve gradually into a totally unregulated market as old gas becomes less of a factor in the aggregate national gas supply. Old gas subject to continuing price ceilings is expected to account for only about one-half of aggregate supply in 1985, with its proportional contribution to national supply diminishing every year. [Emphasis added]

Pierce, *Natural Gas Regulation, Deregulation and Contracts*, 68 Va. L. Rev. 63, 87-89 (1982); *see also*, Pierce, *Reconsidering The Roles of Regulation And Competition In The Natural Gas Industry*, 97 Harv. L. Rev. 345, 348-350 (1983). As explained above, all of the gas with which we are here concerned is deregulated high cost gas, de facto as well as de jure.

able" wellhead sales prices of gas artificially low and had imposed a regulatory maze upon such sales so that production for sale in the interstate market was effectively deterred, all contrary to the national interest in having ready access to an adequate supply of natural gas. *Tenneco, Inc. v. Sutton*, 530 F.Supp. 411, 420 (M.D.La. 1981).

However important the congressional policy and context may be, our precise question today is whether - following enactment of NGPA - federal preemption (with respect to deregulated high cost gas) which undoubtedly existed theretofore continued. Transco argues vigorously that FERC jurisdiction still exists (although in altered form), and that preemption under *Northern Natural* remains the order of the day. Coastal and the other producers candidly pose the issue

> "We will not mince words: if the "first sale" (the wellhead sale) of deregulated gas continues to be subject to FERC's jurisdiction under Section 1(b) of the NGA, then *Northern Natural* applies to this case and Order No. 409-82 is invalid."
>
> —(Brief of Coastal Exploration, Inc., served November 29, 1983, at 22)

Northern Natural held invalid a ratable take order which the Kansas Corporation Commission had entered against an interstate pipeline company. The basis of the decision was state's invasion of the FPC's exclusive regulatory jurisdiction under Section 1(b) of the Natural Gas Act of 1938:

> "We disagree with the Kansas Supreme Court, for we hold that the State Commission's orders did invade the exclusive jurisdiction which the Natural Gas Act has conferred upon the Federal Power Commission over the sale and transportation of natural gas in interstate commerce for resale."
>
> —372 U.S. at 89, 83 S.Ct. at 649, 9 L.Ed.2d at 606.

It is our reading of the Natural Gas Policy Act of 1978 that wellhead sales of the sort of gas with which we are here con-

cerned have been effectively deregulated. We are concerned here with high cost natural gas, 15 U.S.C. § 3317(c) (1), which as a matter of law is no longer subject to FERC (formerly FPC) jurisdiction. 15 U.S.C. § 3431(a) (1) (B) (i). Congress has declared that the first sale of deregulated gas is never made subject to the Natural Gas Act or to FERC's jurisdiction under that act, and "dedicated gas" which is determined to be deregulated gas ceases to be subject to the NGA or FERC's jurisdiction under the NGA. With respect to this category of gas, the regulatory situation existing at the time *Northern Natural* was decided has thus been altered radically.

NGPA Section 601(a) (1) (A), (B) and (D), 15 U.S.C. § 3431(a) (1) (A), (B) and (D), provide as follows:

SECTION 601. COORDINATION WITH THE NATURAL GAS ACT—

(a) JURISDICTION OF THE COMMISSION UNDER THE NATURAL GAS ACT.—

(1) SALES.—

(A) NATURAL GAS NOT COMMITTED OR DEDICATED—*For purposes of section 1(b) of the Natural Gas Act*, effective on the first day of the first month beginning after the date of the enactment of this Act, *the provisions of the Natural Gas Act and the jurisdiction of the Commission under such shall not apply to natural gas which was not committed or dedicated to interstate commerce as of the day before the date of the enactment of this Act* solely by reason of any first sale of such natural gas.

(B) COMMITTED OR DEDICATED NATURAL GAS—Effective beginning on the first day of the first month beginning after the date of the enactment of this Act, *for purposes of section 1(b) of the Natural Gas Act, the provisions of such Act and the jurisdiction of the Commission under such Act shall not apply solely by reason of any first sale of natural gas which is committed*

> *or dedicated to interstate commerce as of the day before the date of the enactment of this Act and which is—*
>
> (i) *High-cost natural gas* (as defined in Section 107(c)(1), (2), (3), or (4) of this Act); [Emphasis added].

The "Joint Explanatory Statement of the Committee on Conference" of the Congress, which accompanied the NGPA, makes clear what the conferees intended that Section 601(a) (1) accomplish.

> "The Conference Agreement limits the jurisdiction of the Commission under the Natural Gas Act in a manner similar to the House-passed bill. Natural gas not committed or dedicated to interstate commerce as of the day before the date of the enactment of this Act is never made subject to the Commission's jurisdiction under sec. 1(b) of the Natural Gas Act. The Commission's jurisdiction under section 1(b) of the Natural Gas Act ceases on the first day of the first month beginning after the date of enactment of this Act for the following categories of natural gas:
>
> High-cost natural gas which qualifies for deregulated price treatment under section 107(c) (1), (2), (3), or (4); [Emphasis added].
>
> * * *

Section 601(a) (1) [15 U.S.C. § 3431(a) (1)] means what it says—the Natural Gas Act of 1938 (NGA) and FERC's jurisdiction under the Act *never* apply to deregulated gas, and certain other categories of gas. That message is decisive of the preemption issue in this case. The reason the Supreme Court voided the ratable take order in *Northern Natural* was because at that particular point in time such an order substantially affected gas which was subject to the FPC's (FERC's) jurisdiction under the NGA. If the NGA and FERC's jurisdiction under the NGA no longer extend to deregulated gas, and FERC has no authority to regulate the first sales and purchases of deregulated gas either directly or indirectly, then *Northern Natural* does not dictate a preemption of otherwise existing state authority.

We are not unmindful of the fact that FERC still has the authority to determine whether pipelines such as Transco may "pass through" the prices they pay at the wellhead, although pass through may be denied only where FERC "determines that the amount paid [by the pipeline] was excessive due to fraud, abuse or similar grounds". 15 U.S.C. § 3431(c) (2). Transco cites this continuing pass through approval authority and urges that FERC jurisdiction continues, only FERC now regulates by reference to a "fraud and collusion" standard as distinguished from the old "just and reasonable" standard. A change in the standard, Transco argues, does not alter the de jure existence of jurisdiction the effect of which is preemption.

The argument is disingenuous. FERC to be sure has today authority to prohibit a pipeline from passing through to consumers excessive wellhead prices paid producers as a result of some nefarious scheme to defraud a consumer. But FERC has no authority to intervene when the pipeline, denied pass through, seeks to get out of its deal with the producers. Though the price paid at the wellhead may well be FERC-determined excessive as the product of fraud or collusion when pass through is sought, it remains a just and reasonable price *as a matter of law* as between the pipeline and the producer. 15 U.S.C. § 3431(b) (1) (A). Nothing in the pass through provisions of NGPA continues in effect any FERC jurisdiction over wellhead first sales of deregulated natural gas.

Our review of the congressional enactments discloses no explicit preemptive language. Our comparison of Rule 48 with federal law reveals no point of actual conflict. Transco's compliance with Rule 48 would not cause it to act in violation of the spirit or letter of any federal law. Finally, we find nothing in federal law as modified by NGPA which leaves in place a "scheme of federal regulation so pervasive as to make reasonable the inference that Congress left no room for the states to supplement it." *Fidelity Federal Savings & Loan Assn. v. De La Cuesta*, 458 U.S. 141, 153, 102 S.Ct. 3014, 73 L.Ed.2d 664, 675 (1982). As presently constituted federal law fails to generate any spirit, policy or rule with which a natural gas producing

state would collide if it sought to do equity between and among owners in a common pool of deregulated gas by the promulgation or enforcement of a common purchaser or ratable take rule.

Our conclusion that federal jurisdiction and regulation, both the expressed and implicit varieties, have been withdrawn does not *ipso facto* leave the state free to reenter, for

> "a federal decision to forgo regulation in a given area may imply an authoritative federal determination that the area is best left *un*regulated, and in that event would have as much pre-emptive force as a decision *to* regulate."
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> —*Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, ____U.S.____, 103 S.Ct. at 1912, 76 L.Ed.2d at 10 (emphasis in original).

This notion must be taken seriously here. Our context is a congressional fact finding that regulation and price controls, however well intended, have had an effect contrary to the national interest.[10] The Congress has found that regulation of the sale and transportation of natural gas in interstate commerce has had the effect of stifling production for the interstate market. The Congress determined that the national interest would be served in the long run by a different approach, that first sales—wellhead sales—should be deregulated and that the inevitably increased cost of production should be borne by the consumer.

In this context, the Congress certainly had the authority to enact not only a federal plan of deregulation of first sales but also that these sales should be free of state regulation. If federal regulation produces evils inimicable to the national interest, a plethora of state regulations varying from jurisdiction to jurisdiction seems equally capable.

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[10]See Pierce, *Natural Gas Regulation, Deregulation and Contracts*, 68 Va.L.Rev. 63, 69-72 (1982); and Pierce, *Reconsidering the Roles of Regulation And Competition In The Natural Gas Industry*, 97 Harv.L.Rev. 345, 371-372 (1983).

Our study of the terms and provisions of the Natural Gas Policy Act of 1978, however, convinces us that the Congress has not proscribed state regulation of wellhead sales of deregulated gas. However consistent a continued proscription on state regulation might have been with the theoretical underpinnings of deregulation, the Congress in NGPA in 1978 did not ban state regulation of deregulated gas. What, and all, the Congress has done insofar as we are concerned is strip away federal regulatory authority thus leaving in effect and wholly exercisable such state regulatory authority as otherwise exists. The lynchpin that holds *Northern Natural* together having been removed, and not having not been replaced by a congressional enactment that wellhead prices of deregulated gas be left unregulated by the states as well, Transco's preemption claim fails. The states today have the authority to require that an interstate pipeline company take deregulated gas ratably and without discrimination in favor of one owner, operator or producer and against another in the same common source of supply. *Cities Services Gas Co. v. Peerless Oil & Gas Company*, 340 U.S. 179, 185, 71 S.Ct. 215, 219, 95 L.Ed. 190, 201 (1950) Transco's Assignment of Error No. 2 is denied.

A caveat: Today's facts and today's holding concern "deregulated gas". The Harper Sand Gas Pool lies at a depth of more than 15,000 feet below the surface of the earth. The wells in issue produce "high-cost natural gas", 15 U.S.C. § 3317(c) (1), with respect to the wellhead sales pricing of which FERC has no jurisdiction. 15 U.S.C. § 3431(a) (1) (B) (i). The first sales of many other categories of natural gas remain subject to FERC jurisdiction and regulation according to NGPA. Nothing said here, of course, can decide any preemption question that may hereafter arise in the context of regulated natural gas produced in this state.

B. The Negative Commerce Clause

By virtue of the Constitution's having vested the Congress of the United States with the power to regulate commerce among

the states, U.S. Const., art. I, § 8, cl. 3, Transco argues via Assignment of Error No. 3 that the State of Mississippi is without authority to enforce Rule 48 as interpreted in Order No. 409-82 because it creates an impermissible burden on interstate commerce.

Grammatically speaking, the Commerce Clause is an affirmative grant of power to the Congress. A century and a half of constitutional decisional jurisprudence, traceable to a dictum by Chief Justice Marshall in *Gibbons v. Ogden*, 22 U.S. (9 Wheat) 1, 209, 6 L.Ed. 23, 73 (1824), have established the legitimacy and reality of the negative Commerce Clause. Even in the absence of exercise by the Congress of its power to regulate commerce, the clause stands as a barrier to the enforcement by the states of laws, statutes or regulations which unreasonably discriminate in favor of in-state interests.

The values undergirding the negative Commerce Clause were articulated by Justice Robert H. Jackson on *H. P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 69 S.Ct. 657, 93 L.Ed. 865 (1949).

> "Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his export, and no foreign state will by customs duties or regulations exclude them. Likewise, every consumer may look to the free competition from every producing area in the Nation to protect him from exploitation by any."
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> —336 U.S. at 539, 69 S.Ct. at 665, 93 L.Ed. at 875.

The Commerce Clause is said to create a national common market. Individual business entities are free to operate commercially in any state where such operations are legal and may not be denied access to markets or resources based upon that choice. Conversely, a buyer's state of origin generally should not affect his access to goods produced anywhere in the coun-

try. The states are without authority to enforce laws imposing substantial burdens on such consumer. *South-Central Timber and Development, Inc. v. Wunnicke*, ____ U.S. ____, 104 S.Ct. 2237, 2247, 81 L.Ed.2d 71, 76 (1984); *Hughes v. Oklahoma*, 441 U.S. 322, 326, 99 S.Ct. 1727, 1731, 60 L.Ed.2d 250, 255-56 (1979); *H. P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 534-538, 69 S.Ct. 657, 663-64, 93 L.Ed. 865, 872-74 (1949); *Cooley v. Board of Wardens*, 53 U.S. (12 How.) 299, 319, 13 L.Ed. 996, 1004-05 (1851).

Any regulation of a business enterprise engaged in interstate commerce has *some* effect on commerce among the states. This is undoubtedly so in the case of Rule 48 and Order No. 409-82. The question is not whether the state's regulations impose a burden on interstate commerce but whether the burden which is imposed is a constitutionally impermissible one.

Just how much of a burden upon interstate commerce must be found before a state runs afoul of the negative Commerce Clause has been a subject of long debate and varying answers by the Supreme Court. This has particularly been so in the past decade or so as the Supreme Court has muddled its way along through the quagmire of a conceptually pleasing but practicably nightmarish (at least from the point of view of achieving rationally consistent results from case to case and thus affording the needed tools to states and citizens concerned with predictability) balancing of interests test first announced in *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 90 S.Ct. 844, 25 L.Ed.2d 174 (1970). In *Pike* the Supreme Court articulated what has become the contemporary formulation of the negative Commerce Clause as applied to a state's attempt to regulate interstate commerce.

> Although the criteria for determining the validity of state statutes [regulations, rules or orders] affecting interstate commerce have variously stated, the general rule that emerges can be phrased as follows: where the statute [regulation, rule or order] regulates even-handedly to

> effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. [citation ommitted] If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate commerce."
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> —397 U.S. at 142, 90 S.Ct. at 847, 25 L.Ed.2d at 178-79.

We have been authoritatively instructed in this formulation of the negative Commerce Clause in *Great Atlantic and Pacific Tea Co. v. Cottrell*, 424 U.S. 366, 371-372, 96 S.Ct. 923, 928, 47 L.Ed.2d 55, 61 (1976). In that case the Supreme Court, reversing a decision of this Court, applied the balancing of interests test and invalidated a Mississippi restriction on the sale of milk as this state had sought to enforce it against a Louisiana milk producer.

A review of the dozens of decisions since *Pike v. Bruce Church*, wherein the established formulation has been rotely recited, produces little in the way of doctrinal consistency or easily rationalized results. Just what is "a legitimate public purpose" and how much of one need exist before a state regulation will be sustained seems almost to depend on who is doing the looking and what that justice had for breakfast on the day of decision; the same with whether the inevitable burden on interstate commerce is "only incidental" or is "clearly excessive".

In the first years of litigation under the new balancing test, the Supreme Court seemed relatively easily satisfied that a burden was excessive and relatively hard to convince that the state did not have a nondiscriminatory alternative adequate to protect local interests. *See Hughes v. Oklahoma*, 441 U.S. 322, 339, 99 S.Ct. 1727, 1737-38, 60 L.Ed.2d 250, 263 (1979) (statute invalid that forbid export of minnows); *Hunt v. Washington*

State Apple Advertising Commission, 432 U.S. 333, 353, 97 S.Ct. 2434, 2446-47, 53 L.Ed.2d 383, 400-01 (1977) (statute invalid that mandated apples be ungraded); *Great Atlantic and Pacific Tea Co. v. Cottrell*, 424 U.S. at 377, 96 S.Ct. at 931-31, 47 L.Ed.2d at 64 (1976) (Mississippi statute invalid that prohibits importing milk from another state unless that state allows Mississippi milk to be imported).

More recent cases give the states wider berth. *See, e.g., Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, ____U.S.____, 103 S.Ct. 1905, 1917-18, 76 L.Ed.2d 1, 16-18 (1983) (state commission could govern wholesale electric rates); *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456, 471-73, 101 S.Ct. 715,727-29, 66 L.Ed.2d 659, 673-75 (1981) (state could ban sale of milk in plastic containers); *Reeves, Inc. v. Stake*, 447 U.S. 429, 443-47, 100 S.Ct. 2271, 2281-82, 65 L.Ed.2d 244,255-57 (1980) (state could limit sale of state-owned cement to residents); *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 127-29, 98 S.Ct. 2207, 2214-15, 57 L.Ed.2d 91, 101-02 (1978) (state could mandate that oil producers not own retail outlets). The same permissive trend is also discernible in recent state taxation of interstate commerce cases, arguably decided via a different doctrinal formulation. *See, e.g., Commonwealth Edison v. Montana*, 453 U.S. 609, 624-29, 101 S.Ct. 2946, 2957-59, 69 L.Ed.2d 884, 898-902 (1981) (state could place exorbitant severance tax on coal); *Complete Auto Transit Co. v. Brady*, 430 U.S. 274, 288-89, 97 S.Ct. 1076, 1083-84, 51 L.Ed.2d 326, 336-37 (1977) (upholding a tax imposed by this state against an interstate trucking company for the privilege of doing business within this state).

One concern arising from the ad hoc interpretation of the negative Commerce Clause is the authoritative effect of pre-*Pike* decisions. We express this concern in the context of Transco's insistence that one of the burdens upon interstate commerce created by the rule and order here in issue is increased prices to the consumer. Pre-*Pike* decisions, however, establish that increased prices or decreased supplies to consumers in other states do not necessarily render a state's

regulation unconstitutional. *Cities Service Gas Co. v. Peerless Oil and Gas Co.*, 340 U.S. 179, 186-87, 71 S.Ct. 215, 219-20, 95 L.Ed. 190, 202-03 (1950) (state could order pipeline to ratably take sellers gas at fixed price); *Parker v. Brown*, 317 U.S. 341, 368, 63 S.Ct. 307, 322, 87 L.Ed. 315, 335-36 (1943) (state could control raisin marketing); and *Milk Control Board v. Eisenberg Farm Products*, 306 U.S. 346, 352-353, 59 S.Ct. 528, 530-31, 83 L.Ed. 752, 756-57 (1939) (state could set minimum price paid to milk producers). With some temerity, we assume that the premise derived from these cases is still good law.

In this context, *Pike v. Bruce Church, Inc.* directs that we proceed to a consideration of what legitimate local interests may be said to undergird and be promoted by Rule 48 and Order No. 409-82.

Coastal, Getty and the other producers argue that conservation of an important natural resource and the prevention of waste are implicated. Without doubt, if this were so, such would be a legitimate local interest entitled to great weight and consideration in the Commerce Clause balancing test. It is difficult, however, for us to see how there is waste of natural resources when an interstate pipe line company refuses to take ratably or otherwise. Waste would seem to follow from taking too much, not too little.

We are aware of the statutory definition of waste. Miss. Code Ann. § 53-1-3(k) (Supp. 1983). How our Legislature defines waste for purposes of the Mississippi Conservation Act, of course, is its prerogative. *Compare Stong, Administratrix v. Freeman Truck Line, Inc.*, ____ So.2d ____, ____ (Miss. 1984); *McLaurin v. Mississippi Employment Security Commission*, 435 So.2d 1170, 1171-1172 (Miss. 1983). Its definition, of course, is in no way controlling for purposes of analysis under the Commerce Clause of the Constitution of the United States.

The true and entirely legitimate local interest here implicated is fairness. Rule 48 is a rule of equity. The drainage phenomenon is a fact of life of natural gas production. *Shell Oil Company v. James*, 257 So.2d 488, 494-495 (Miss. 1971). The

state through its Oil and Gas Board has acted in this and other ways to assure equity and fairness between and among the varying interests in a common source of supply. *See Phillips Petroleum Co. v. Millette*, 221 Miss. 1, 15-17, 72 So.2d 176, 179 (1954) (protection against loss through drainage required by fundamental notions of equity and justice).

We regard fairness as among the more noble purposes of the state. It is a fundamental component of the idea of justice. Rawls, *A Theory of Justice* (1971). That we are concerned here with the distribution of material and highly valuable resources does not denigrate or render less noble the state's duty to assure fairness between all persons affected. A laudable feature of Rule 48 in the present context is that it applies to owners of interests in the common source of supply without reference to whether they be Mississippians. Getty is entitled to the same fair treatment as is Coastal as are the Fairchilds as is Tomlinson and as is Inexco and so forth.

Transco argues that the principal burden upon interstate commerce resulting from Rule 48 and Order No. 409-82 is higher prices to the ultimate purchasers and consumers of natural gas. The argument is not persuasive.

First, as indicated above, we believe the proposition well-established that higher prices to consumers in another state do not render a state's regulation of commerce impermissible per se under the negative Commerce Clause. *Cities Service Company v. Peerless Oil and Gas Co.*, 340 U.S. 179, 186-87, 71 S.Ct. 215, 219-20, 95 L.Ed. 190, 202-03 (1950); *Parker v. Brown*, 317 U.S. 341, 368, 63 S.Ct. 307, 322, 87 L.Ed. 315, 335-36 (1943); *Milk Control Board v. Eisenberg*, 306 U.S. 346, 352-353, 59 S.Ct. 5[illegible], 530-31, 83 L.Ed. 752, 756-57 (1939).

Second, the Congress has declared that all reasonable costs of production of natural gas shall be borne ultimately by the consumer. This is one of the fundamental policy determinations underlying the Natural Gas Policy Act of 1978. Indeed, it was assumed by Congress that prices to the consumer would increase. This was found preferable to the pre-existing price

controls and regulatory policies of FERC under the pre-1978 Natural Gas Act. Thus, whether increased prices to consumers may be fairly characterized as an incidental burden upon interstate commerce, we find it persuasive that Congress within the scope of its power under the affirmative Commerce Clause has expressly authorized such increases.

Transco further argues that there is a burden on interstate commerce emanating from Rule 48 in that compliance with Order No. 409-82 will require that more natural gas be taken from Mississippi and less from Louisiana and Texas. The quick answer is that Louisiana and Texas also have ratable take regulations in effect.[11] Furthermore, no evidence has been adduced which would lend credence to Transco's argument that Rule 48 impermissibly discriminates against natural gas production in Louisiana and Texas.

The fundamental flaw in Transco's reasoning on the burden point is that it seems to be talking much more about a burden upon Transco than a burden upon interestate commerce. The burden upon Transco appears traceable to its contract with Getty, not to Rule 48. That contract is one Transco freely and voluntarily entered with Getty. It is hard to see how a ratable take rule or order could be said to generate an unreasonable burden on interstate commerce when the only thing requiring Transco (or any other interstate pipeline) to take at all, ratably or otherwise, is its own contract.

Many important provisions of that contract reflect that the parties carefully considered future eventualities. The so-called take-or-pay provision obligating Transco to pay whether it takes the production made available by Getty is one such

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[11]Other natural gas producing states have comparable ratable take regulations sometimes referred to as "common purchaser" statutes. Kan. Stat. Ann. § 55-703 (Supp. 1983) (Kansas); La. Rev. Stat. Ann. § 30:42 (West Supp. 1984) (Louisiana); Neb. Rev. Stat. § 57-907 (1979) (Nebraska); N.M. Stat. Ann. § 70-2-19 (Supp. 1984) (New Mexico); N.D. Cent. Code § 49-19-07 (1978) (North Dakota); Okla. Stat. Ann. tit. 52, § 23 and 233 (West 1969) (Oklahoma); Tex. Nat. Res. Code Ann. § 11.083 (Vernon 1978) (Texas).

clause. Transco's problem is that it failed to protect itself against the market glut and declining prices consumers are willing to pay for natural gas. It is not now and never has been the function of this Court to relieve a party to a freely negotiated contract of the burdens of a provision which becomes more onerous than had originally been anticipated. *Bunting v. Orendorf*, 152 Miss. 327, 332, 120 So. 182, 183 (1929); *Jemison v. McDaniel*, 25 Miss. 83, 86 (1852); *Gulf Oil Corp. v. Federal Power Commission*, 563 F.2d 588, 598-600 (3d Cir. 1977).

Not only did Transco freely and voluntarily—and no doubt in anticipation of accomplishing its own advantage—enter into the contract with Getty in 1980, it did so against the backdrop of Rule 48. One Transco official admitted actual knowledge of Rule 48. In any event, an interstate pipeline such as Transco is chargeable with full knowledge of Rule 48 and any other applicable state regulations (or statutes, laws, etc.) existing at the time of contracting. The parties contract against the backdrop of regulation and ought generally be held to an implied incorporation of applicable regulations into the contract.

Transco's argument that Rule 48 had never been enforced is lame indeed. Transco knew of the existence of the rule or was certainly charged with knowledge of its existence; the rule has been on the books since 1952. Despite the argument made here, Transco was chargeable with knowledge that the states became entitled to play a greater role in regulation of the production of deregulated natural gas following enactment of the Natural Gas Policy Act in 1978. More fundamentally, Transco was certainly aware of the drainage problem inherent in natural gas production when there are two or more wells producing from a common source of supply, thus necessitating a rule something like Rule 48 to assure equity and fairness amongst the owners of the various interests in the common pool.

Transco has the right to pass the costs it incurs in purchasing natural gas through to the consumer. 15 U.S.C., § 3431(c). In this sense, it is not Transco who experiences a burden, it is the

consumer. If higher purchasing prices at the wellhead lead to higher prices to the consumer and a loss of markets, this is simply one inevitable consequence of the free market policies of the era of deregulation with respect to which Transco is vested by the negative Commerce Clause with no right to complain.

A final point by Transco here is that the state had a less discriminatory alternative adequate to protect local interest, i.e., a ratable production order as distinguished from a ratable take order. To be sure, one inquiry under the *Pike v. Bruce Church* balancing test is whether there are available to a state less discriminatory alternatives adequate to protect the local interests implicated, and the Supreme Court has made it clear that this inquiry must be taken seriously. *Hughes v. Oklahoma*, 441 U.S. at 339, 99 S.Ct. at 1737, 60 L.Ed.2d at 263; *Hunt v. Washington State Apple Advertising Commission*, 432 U.S. at 353, 97 S.Ct. at 2446-47, 53 L.Ed.2d at 400-01; *Great Atlantic and Pacific Tea Co. v. Cottrell*, 424 U.S. at 377, 96 S.Ct. at 930-31, 47 L.Ed.2d at 64.

The search for such alternatives, however, need not be made in connection with our Commerce Clause inquiry until it first be established that the regulation in question creates an unreasonable burden on commerce. This Transco has failed to do—for as explained above, the burdens are on Transco, not interstate pipe lines generally, because only Transco has, wittingly or unwittingly, bound itself to a long term, fixed price gas purchase contract. When that contract is taken out of the case, it is seen that the so-called burdens of Rule 48 disappear.

The point is made crystal clear by Transco's present policy of insisting upon "market-out" provisions in its contract—provisions which allow the price Transco pays to the producer to fluctuate with market price to the consumer. If Transco had negotiated a market-out clause in its contract with Getty, these proceedings no doubt would not be before this Court today.

In summary, we hold that the State of Mississippi via its Oil and Gas Board had the authority to promulgate and has the authority to enforce Statewide Rule 48. Nothing in Rule 48 or

its interpretation in Order No. 409-82 contravenes the authority remaining vested in the State of Mississippi once its authority to regulate commerce has been effectively restricted by the negative Commerce Clause. Transco's Assignment of Error No. 3 is rejected.

C. Void-For-Vagueness

Under Assignment of Error No. 4, Transco argues that Rule 48 is void for vagueness. The claim is predicated upon rights said to be vested in Transco by virtue of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States.

It is the foremost requisite of a legal system that there be general rules. Where those rules are not made clear and are not published and available to persons in the planning of their economic and social activities, the efficacy of the system is in substantial danger. Fuller, *The Morality of Law*, 46-51, 63-70 (rev. ed. 1969).

These notions have acquired constitutional status. *Connally v. General Construction Co.*, 269 U.S. 385, 46 S.Ct. 126, 70 L.Ed. 322 (1925) states

> "[A] statute which either forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application violates the first essential of due process."
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> - 269 U.S. at 391, 46 S.Ct. at 127-28, 70 L.Ed. at 328.

An unconstitutionally vague statute or regulation is unenforceable. *A. B. Small Co. v. American Sugar Refining Co.*, 267 U.S. 233, 242, 45 S.Ct. 295, 298, 69 L.Ed. 589, 594-95 (1924).

Most of the void for vagueness cases have arisen in the context of criminal prosecutions. *See ABC Interstate Theatres, Inc. v. State*, 325 So.2d 123, 125 (Miss. 1976) (obscenity statute overbroad). It is clear, however, that the doctrine applies to

civil statutes and to regulations. *See A. B. Small Co. v. American Sugar Refining Co.*, 267 U.S. at 237, 45 S.Ct. at 296, 69 L.Ed at 592 (applied to civil statute); *Hynes v. Mayor of Oradell*, 425 U.S. 610, 620, 96 S.Ct. 1755, 1760, 48 L.Ed.2d 243, 253, (1976) (applied to regulation). On the other hand, when the doctrine is applied in the context of economic regulation its strictures are relaxed. *Village of Hoffman Estates v. Flipside, Hoffman Estates, Inc.*, 455 U.S. 489, 498, 102 S.Ct. 1186, 1192, 71 L.Ed.2d 362, 371-372 (1982).

A rule or standard is not objectionable merely because it is stated in general terms and is not susceptible of precise application. Familiar examples of such general standards abound in our law, *e.g.*, negligence, unconscionability, fraud. We doubt anyone would seriously argue today that these standards are unconstitutionally vague.

Transco focuses its attack upon three aspects of Rule 48. These are (a) "ratable take", (b) "purchase without discrimination", and (c) "same common source of supply". We find these terms readily understandable. Transco's brief demonstrates that they are not susceptible of precise mechanical application, but what law is?

Ratable take suggests a general rule of equity. The phrase refers to the taking of an amount of gas from one well such that the percentage of said amount to the well's allowable is the same as the percentage that the amount taken from a second well bears to the allowable for the second well. Ratable taking connotes fairness. Its synonym is "pro-rata". *HBOP, Ltd v. Delhi Gas Pipe Line Corporation*, 645 P.2d 1042, 1046 n.9 (Okla. Ct. App. 1982).

The concept as we understand it refers to production. It refers to the percentage of allowable production of a common source of supply. It also refers to equity between interests in a given pool. It means that the party "taking" must take pro-rata with respect to the relative interests, percentage-wise, the various owners have in the pool. That the concept is general hardly establishes that it is impermissibly vague.

The phrase "purchase without discrimination' imparts the same meaning. At the risk of being repetitious, purchase without discrimination means to purchase or acquire pro-rata from a given pool the same percentage of one owner's interest as is purchased of another owner's interest. It likewise means, within a given pool or common source of supply, that the party purchasing will purchase the same percentage of one well's allowable as is the case with respect to all other wells in the pool or common source of supply.

We pause here to note that a central question in this case is whether Transco may purchase without *price* discrimination with respect to the varying interests in the six wells said to be in a common source of supply. As we explain below, the Legislature has not vested the Oil and Gas Board authority to proscribe price discrimination or to inaugurate any other form of regulation of the prices of wellhead sales of natural gas. This is not to say that the Legislature could not endow the Oil and Gas Board with such authority, if it rationally determined that such was consistent with the public interest. We simply hold today that it has not yet done so.

Finally, Transco challenges as vague the term "common source of supply". This one gives us no trouble. The term simply refers to that geological configuration or area within which a significant drainage problem would result if there be unratable taking from one well to another. It is synonymous with "pool"[12]

The Supreme Court of the United States has decided that a state ratable take order, although couched in general language, presents no constitutional infirmities regarding vagueness. *Phillips Petroleum Company v. Oklahoma*, 340 U.S. 190, 192, 71 S.Ct. 221, 222, 95 L.Ed. 204, 206-07 (1950). We do not regard *Corporation Commission v. Champlin Refining Co.*, 286 U.S. 210, 242-243, 52 S.Ct. 559, 567-68, 76 L.Ed. 1062, 1082-83 (1931) as being to the contrary. Assuming arguendo that

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[12]*See supra* note 4.

Champlin is to the contrary, it has been in part overruled by more recent decisions.

D. Taking Without Compensation

Transco next argues that Order No. 409-82 is an arbitrary and unreasonable exercise of the state's police power and, if enforced, would result in a taking of Transco's property without compensation in violation of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States.

It may be true that a taking of private property by governmental action violates the owner's due process rights if the action bears no reasonable relation to a legitimate governmental purpose or is otherwise arbitrary. *Thompson v. Consolidated Gas Utilities Corp.*, 300 U.S. 55, 70, 57 S.Ct. 364, 371, 81 L.Ed. 510, 518 (1936). Here, however, we have a legitimate governmental purpose. The state has a completely legitimate interest, as articulated in the policy statement of the Conservation Act, to

> "safeguard, protect and enforce the co-equal and correlative rights of owners in a common source or pool of oil and gas to the end that each such owner in a common pool or source of supply of oil and gas may obtain his just and equitable share of production therefrom."

As discussed previously, it is Transco's contract with Getty - not Rule 48 - which effects a "taking" of Transco's property. This sort of "taking" is colloquially known as "business".

We reject out-of-hand Transco's argument that Order No. 409-82 constitutes an impermissible taking of private property without compensation and in so doing we complete our determination that the claims advanced by Transco based in federal law are without merit.

V. TRANSCO'S CLAIMS UNDER STATE LAW

A. The Board's Authority To Promulgate A Ratable Take Rule

Turning to the state law claims, Transco first argues that the Oil and Gas Board was without authority to adopt or enforce a

rule requiring ratable taking such as Rule 48. The point is without merit.

The State Oil and Gas Board is a creature of the legislature and, of course, has no authority other than that vested in it by statute. *Masonite Corporation v. State Oil and Gas Board*, 240 So.2d 446, 449 (Miss. 1970). To ascertain what authority the Board has, we consult the Mississippi Oil and Gas Conservation Act of 1948, originally enacted as House Bill No. 80, Miss. Laws of 1948, Chapter 256, and now codified as amended as Miss. Code Ann. § 53-1-1, et seq., (Supp. 1983).

Looking to the words of that enactment we find in Section 53-1-17(c) Board authority to carry out the general policy directives of Section 53-1-1 which are, in part, that the co-equal and correlative rights of owners in a common source or pool of oil and gas shall be safeguarded to the end that each such owner in a common pool or source of supply of oil and gas may obtain his just and equitable share of production therefrom. *Barnwell, Inc. v. Sun Oil Company*, 249 Miss. 398, 406, 162 So.2d 635, 638 (1964).

An understanding of the legislative words emerges from thought about what co-equal and correlative rights such owners have under our law and just why and from what these rights need protection.

Our core concern, at the risk of repetition, is the geological phenomenon of drainage, described in *Shell Oil Company v. James*, 257 So.2d 448 (Miss. 1971) in this way.

> When the pool of oil has been penetrated by a recovery well, the oil and gas located in the pool move from a high pressure area to a low pressure area so that the oil and gas migrate from the property of one landowner to another. This exodus is called drainage. 257 So.2d at 494-495.

In this context we understand the correctness of the observations in one of the leading treatises on oil and gas law, *Summers on Oil and Gas*, Vol. IA, § 103.1 at 132:

> The mere opportunity of a landowner to take his share of the oil and gas in a common source of supply does not provide complete protection of his property rights in them. If others produce and market, he must also produce and market or lose much of his share through drainage and the exhaustion of reservoir energy. He cannot produce and market unless a market outlet is available. To provide market outlets for both oil and gas a few states have enacted common purchaser statutes requiring common carrier pipelines or other persons in business of purchasing oil or gas in a common source of supply to take ratably from all owners.

The geological realities of the world of oil and gas have sensitized the lawmakers of this state. *Phillips Petroleum Co., v. Millette*, 221 Miss. 1, 15-17, 72 So.2d 176, 179 (1954) recognizes that the prevention of loss through drainage is required by fundamental notions of equity and justice. Our law has long ago translated these notions of equity and justice into enforceable rights vested in owners of interests in oil and gas rich lands. *Shell Oil Company v. James*, 257 So.2d 488, 495 (Miss. 1971). It is of such rights that our Legislature speaks when it declares in Section 53-1-1 the public policy of the state that "the co-equal and correlative rights of owners in a common source or pool" be protected. Similarly the Legislature speaks of such rights when Section 53-1-17(c) authorizes the Board to carry out the general policy directives of Section 53-1-1.

Being as redundant as occasionally are judges, our legislators have in Section 53-1-17(c)(12) vested the Oil and Gas Board with the authority to prevent abuse of these correlative rights which may result from non-uniform, disproportionate or unratable withdrawals causing undue drainage between tracts of land or resulting in one or more owners in such pool producing more than his just and equitable share of the production from such pool.

Moreover, the Board has the authority under Section 53-1-17(c)(13) to "prevent, so far as practicable, reasonably

avoidable drainage from each developed unit which is not equalized by counter-drainage." *Shell Oil Company v. James*, 257 So.2d 488, 493 (Miss. 1971).

Beyond that, the Board has implied authority to do what may be reasonably necessary to carry out the specific mandates of the Legislature. *State Oil and Gas Board of Mississippi v. Brinkley*, 329 So.2d 512, 514-515 (Miss. 1976); *Mississippi Public Service Commission v. Chambers*, 235 Miss. 133, 142, 108 So.2d 550, 554 (1959).

Couple all of this with the provisions of Section 53-1-17(c) which empower the Oil and Gas Board to make "such reasonable rules, regulations and orders as may be necessary from time to time in the proper administration and enforcement" of the oil and gas conservation laws of this state, *State Oil & Gas Board v. Mississippi Mineral & Royalty Owners Association*, 258 So.2d 767, 768 (Miss. 1971), and we have more than ample statutory authority vested in the Board enabling the promulgation and enforcement of a rule requiring ratable taking such as Rule 48.

We have upheld the authority of the Board to promulgate a variety of rules with respect to which arguably there is less express statutory authorization than is the case here. *See, e.g., Barnwell, Inc. v. Sun Oil Co.*, 249 Miss. 398, 406-07, 162 So.2d 635, 638 (1964) (Board has power to allocate and apportion production); *Frost v. Gulf Oil Corp.*, 238 Miss. 775, 791-92, 119 So.2d 759, 764 (1960) (Board rules supplement statute); *Corley v. Mississippi State Oil & Gas Board*, 234 Miss. 199, 211-13, 105 So.2d 633, 638 (1958) (perpetuation of 40 acre units and creation of field-wide unit upheld because the units would protect the co-equal and corelative rights of the owners); *Hassie Hunt Trust v. Procter*, 215 Miss. 84, 97-98, 60 So.2d 551, 556 (1952) (Board could designate drilling units); *Green v. Superior Oil Co.*, 59 So.2d 100, 101 (Miss. 1952) (upholding Board's spacing rules providing 320 acre units).

Requiring one such as Transco to take what it does not want should not be done lightly. The right to purchase what one

wants (at a negotiated price) and to decline the purchase of what one does not want is normally secured, absent extraordinary circumstances. One the other hand, the general contours of the police power of the state have become well-established, and that power may qualify rights otherwise secured.

In *Superior Oil Company v. Foote*, 214 Miss. 857, 59 So.2d 85 (1954), this Court, speaking of the exercise of the police power as vested in the Board, had this to say:

> The police power of the state includes not only regulations to promote public health, good morals, and good order, but also the . . . [authority] to regulate and to promote development of industry and utilization of natural resources in order to add to the wealth and prosperity of the state. 214 Miss. at 875, 59 So.2d at 93.

A corollary desideratum equally susceptible of lawful achievement via the state's police power calls for a currently fair division of those natural resources. This the policy statement of Section 53-1-1 proclaims when it declares it in the public interest to safeguard, protect and enforce the co-equal and correlative rights of owners in a common source of supply. This our Court has embraced when, in *Superior Oil Co. v. Foote*, we recognized that in the lawful exercise of its police power

> the state may enact regulatory laws for and proscribe methods of extracting oil and gas for the . . . protection of the correlative rights of all owners in a common source of supply. 214 Miss. at 876, 59 So.2d at 93.

Accepting values from our past, our law continues to cherish freedom of contract and freedom to contract. U.S. Const. art. I, § 10, cl. 1; Miss. Const. art. III, § 16 (1890). Those freedoms, however, are not unqualified. This Court has repeatedly recognized that ordinary economic freedoms generally secured are

> qualified by a proper exercise of the police power of the state. . . . Hence it is said that all contract and property

> rights are subject to a reasonable exercise of the police power.

Superior Oil Co. v. Foote, 214 Miss. at 876, 59 So.2d at 93; *Mississippi Milk Commission v. Vance*, 240 Miss. at 857, 129 So.2d at 661.

The Supreme Court of the United States has likewise recognized that the prohibitions of the facially absolute Contract Clause

> must be accommodated to the inherent police power of the State "to safeguard the vital interests of its people".

Energy Reserves Group, Inc. v. Kansas Power and Light Company, ____ U.S. ____, 103 S.Ct. 697, 704, 74 L.Ed.2d 569, 580 (1983).

The Legislature of this state has lawfully empowered the State Oil and Gas Board to protect the co-equal and correlative rights of owners in a common pool of natural gas. The Board's ratable take rule is a proper exercise of the authority so vested in it.

Without further ado, we hold that the State Oil and Gas Board has the authority to promulgate a rule requiring ratable taking, such as Rule 48, and has the authority to enforce that rule according to its tenor. We affirm so much of the order of the State Oil and Gas Board as requires Transco, if it takes at all from a common source of supply, to take ratably; that is, Transco is required to offer in good faith to purchase from every one of the various producing interests in the common source of supply[13] the same percentage of those producers' gas as it

[13]This is as good a spot as any to note our concern that we may not know accurately how many wells are in the common pool or common source of supply, i.e., how many wells are subject to drainage if Transco continues to take 100 percent of the allowable from the two Florida Exploration wells. The Board finds as a fact that the six wells: (1) Getty-Rogers, (2) Getty-Sipp, (3) Getty-Buckley, (4) Tomlinson-Willoughby, (5) Florida-Carlisle and (6) Florida-Barnes are producing from a common pool. Getty offered convincing proof that there may be others, and we find nothing in the Board's finding of fact which rejects that proof. Should there be other producers or owners who are suffering drainage, they will have to make that fact known to the appropriate tribunal before they may be afforded any relief.

purchases from that producer the highest percentage of whose interest Transco takes.

This is consistent with the language of Rule 48. It is likewise consistent with the authority vested in the State Oil and Gas Board by the Legislature. It is finally consistent with geological realities and national and state public policy, insofar as we are able to discern them.

Fixing prices, however, is another matter.

F. The Board's Lack of Authority To Regulate Prices or Proscribe Price Discrimination

Order No. 409-82 does not in clear and unequivocal language prohibit Transco's price discrimination. The order does not specifically order Transco to pay all non-contract owners in the common pool the same $7.907 per mmbtu as Transco is paying Getty. The order merely provides that Transco is ordered

(a) to comply with Statewide Rule 48,

(b) if it takes natural gas from the Harper Sand Gas Pool, to "ratably take from the wells producing from the common pool,"

(c) "to ratably take and purchase gas without discrimination in favor of one owner, operator or producer against another in the said common source or pool", and

(d) if it elects to take from the pool, to "ratably take and purchase without discrimination in favor of the operators Getty and Tomlinson against Coastal, the Fairchilds, and Inexco".

It is tempting to speculate regarding the reason the Board stuck so close to the exact language of Rule 48 and, by way of contrast, eschewed use of any language expressly proscribing price discrimination and requiring that Transco pay one and all the $7.907 per mmbtu price. Such a proscriptive order would hardly wash when Transco is paying Tomlinson $6.511 per mmbtu, and Florida Exploration $8.4066, and Sabine $5.00; and so forth—all in the same common source of supply. More fundamentally, the Board's choice of wording in Order No.

409-82 telegraphs its own uneasiness about its authority to regulate prices or prohibit price discrimination.

Notwithstanding the arguable vagueness of the order, everybody has construed it to proscribe Transco from further discrimination in price paid producers in the common pool. For example, Coastal's brief before this Court states

> "At the trial, we *all* knew that the issue was price . . . The record is literally replete with statements by Transco's counsel and witnesses that the *only* issue was price."
>
> —(Brief of Coastal Exploration, Inc., served November 29, 1983, at 66)

Our review of the record and the course of proceedings before the Board, and subsequently the Circuit Court, together with our study of the briefs of the parties, convinces us that *price* is and from the outset has been a major issue in this controversy. It is in this context that we turn to Transco's next argument, to-wit: Assuming *arguendo* that the Oil and Gas Board has lawfully required ratable taking, the Board has no authority to regulate or proscribe differences in price. In large part, we agree.

Our approach is the same as before. The Board has only that authority which the legislature has constitutionally and lawfully vested in it. Our question becomes, has the Legislature vested the Board with authority to fix wellhead or first sale prices purchasers such as Transco must pay for the gas they take?

Before it may be sustained, the price regulation feature of Order No. 409-82 must find its undergirding authority in the enactments of the Legislature. *Masonite Corporation v. State Oil and Gas Board*, 240 So.2d 446, 449 (Miss. 1970). Order No. 409-82 may not be validated solely by reference to the language of Rule 48 for the obvious reason that the Board may not give one of its rules a construction beyond the scope of the enabling authority emanating from the Legislature.

Our point of inquiry is *not* whether the State of Mississippi acting through its duly constituted Legislature has the authority to engage in price regulation. This authority lies well within what is commonly referred to as the police power of the state. *Nebbia v. New York*, 291 U.S. 502, 54 S.Ct. 505, 78 L.Ed. 940 (1934); *Mississippi Milk Commission v. Vance*, 240 Miss. 814, 855, 129 So.2d 642, 660 (1961). We are concerned with the narrower question whether the Legislature has vested the Board with authority to make or enforce price regulation measures such as those found in Order No. 409-82. In search the answer we again consult the Mississippi Oil and Gas Conservation Act of 1948, as amended, and that source only.

Keep well in mind the general policy of this state and this nation: that prices for the sale of goods or services ought to be the product of an arms-length bargain in particular and of the market place in general. Price regulation measures remain the exception. Because they are the exception and because they do violence to the generally valid values and economic realities represented by such catch phrases as "freedom of contract" and "supply and demand", price regulation measures must be authorized in clear and unmistakeable language.

The authority to regulate prices is a drastic departure from the norm. It may never be left to implication. If it has not been expressed, it does not exist.

This state today regulates the price paid by the consumer for electricity, natural gas and telephone service. Insurance premiums are also the subject of state regulation. In each of these instances the authority to regulate is delegated to the administrative agency in clear and unmistakeable language. A familiar example of this from the not too distant past is the Mississippi Milk Commission Act, Senate Bill No. 1757, chapter 155, Laws of 1960. *Mississippi Milk Commission v. Vance*, 240 Miss. 814, 860, 129 So.2d 642, 662-663 (1961).

Against this backdrop we regard the stark contrast presented by the Mississippi Oil and Gas Conservation Act of 1948. First, we find no mention of a need to regulate wellhead sales

prices in the declaration of policy in Section 53-1-1. Beyond that, there is no such authority provided in Section 53-1-17, the statute enumerating the lawful powers of the Board. Not even the newly enacted Section 53-1-17(f)[15] provides any such authorization. Indeed, the word "price" is not used, nor any of its synonyms.

The only mention of the term price in any legislative language empowering the Board appears in Section 53-1-17(c)(17), to wit:

> To make such determinations of oil and/or natural gas maximum lawful ceiling prices as allowed by federal or state law.

The price regulation feature of Order No. 409-82 obviously is not a determination of maximum lawful ceiling prices within Section 53-1-17(c)(17). As indicated at the outset, we are concerned here with deregulated gas.

Turning to the history of the Conservation Act and the Board's experience with it, we again find no hint that the Board has heretofore considered that it has price fixing authority. In part this might be explained by the pre-1978 federal preemption of the pricing of wellhead first sales. *Northern Natural Gas Co. v. State Corporation Commission of Kansas*, 372 U.S. 84, 91-92, 83 S.Ct. 640, 650-51, 9 L.Ed.2d 601, 607 (1963); *Phillips Petroleum Company v. Wisconsin*, 347 U.S. 672, 682-84, 74 S.Ct. 794, 799-800, 98 L.Ed. 1035, 1047-48 (1954). Whatever the reason—because Natural Gas Act of 1938 had preemptive effect, because such price regulation is not needed to give owners adequate and reasonable protections against the perceived evils of drainage, or because collectively the Legislature never thought of the matter, the outcome determinative fact is that the Legislature simply has not vested the Board with authority to fix wellhead first sale prices of natural gas. This is so whether the price fixing be done directly or under the ruse of prohibiting discrimination.

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[15]See Chapter 506, Miss. Laws of 1983, originally House Bill No. 919.

Rule 48 has been promulgated for over thirty years. We are aware of no evidence prior to Order No. 409-82 that the Board has heretofore considered Rule 48 to proscribe price discrimination. The primary prior Board proceeding discussed in the briefs is *In Re Petition of Cenard Oil and Gas Co.*, Docket No. 60-64-92, Order No. 81-64, dated April 16, 1964. In that case the Board correctly found Southern Natural Gas Co.'s refusal to purchase gas from Cenard's two wells completed into a common reservoir at the same rate as it purchased from another to be a violation of Rule 48. The Board's order directing Southern natural to take ratably and otherwise comply with Rule 48 makes no mention of price.

We are loathe to tell an administrative agency how to construe its own rule. In this case the Board has determined to enforce an order in part at least unauthorized by the enabling legislation. In this context it becomes our responsibility to advise the Board that the only lawful interpretation of the rule is that Transco, if it desires to take at all from a common source of supply, must take ratably. With respect to price, that is a matter of private negotiation between the parties. Any owner who wishes to enter into a contract with respect to the sale of his interest is free to do so. If for whatever reason, the owner wishes to "play the market", he is entitled both to the benefits of a high demand market and the burdens of a market glut such as we have now. Any other interpretation of the rule is arbitrary, capricious and unlawful.

All of this is particularly true when it is remembered that the statute has not authorized the Board to engage in price regulation and when it is likewise remembered that the dominant legislative concern was protecting producers and owners from the geological phenomenon of drainage, a far different matter from the economic phenomenon of price discrimination.

Mississippi is not the only natural gas producing state which has determined that requiring ratable taking without any regulation of or prohibition on discrimination in price is a rational state policy. The Louisiana Supreme Court has interpreted

language similar to Rule 48 in its common purchaser statute as applying only to quantity and not price. In *State v. Arkansas Louisiana Gas Co.*, 227 La. 179, 78 So.2d 825 (La. 1955), Arkla was brought to trial for offering only five cents per one thousand cubic feet of gas (mcf)[14] to some when it was paying others 11¢/mcf for gas produced from the same pool. As in this case, the issue was price only. Louisiana's attorneys contended that the term "purchase . . . without discrimination" in the statute must include price differences or else the statute would be meaningless. The court responded:

> . . . We cannot find or discern any prohibition against 'price' discrimination, and we cannot read such a prohibition into the statute. . . .
>
> It is manifest that *the statute was obviously drawn to prohibit discrimination solely in the matter of quantity,* to prevent unfair, discriminatory and inequitable abuses in the distribution of natural gas, not as to prices to be paid, but solely to give security to producers in that they would all stand on an equal footing insofar as access to a market through pipeline facilities would be made available. The statute sought to alleviate and prevent the abuses whereby some producers were favored as against others, some afforded markets, others ignored, and, by the process of prorating among producers, assured them that no one would sell more than the other in a . . . [common source of supply]. 227 La. at 188-89, 78 So.2d at 828 [Emphasis added]

The construction Louisiana's Supreme Court has placed on its ratable take statute, of course, is not controlling here. In determining that the Mississippi Legislature has *not* decided that a regime of price regulation or a prohibition on discrimination in wellhead sales prices are necessary parts of the state's important policy of protecting the "the co-equal and correlative

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[14]The two predominant units of natural gas measurement, one thousand cubic feet (mcf) and one million British thermal units (mmbtu), contain approximately equivalent amounts of energy.

rights of owners in a common source" of supply, although it may well have the authority to so provide, we take comfort from the fact our present law and policy are consistent with what at least one sister natural gas producing state has done.

There is a final reason why we have refused to imply Board authority to regulate wellhead sales prices. For the moment we have difficulty understanding how the sort of price regulation attempted in Order No. 409-82 serves legitimate public interest as distinguished from private self-interests.

Price differentials emanating from arms-length contract negotiations are surely not contrary to the public interest. Many legitimate economic factors may produce such differentials, not the least of which would be the length of the contract, whether the price was fixed or subject to variation, supply and demand and other prevailing and reasonably foreseeable market conditions. The record before this Court reflects 35 contracts ranging from $5.00 to $9.054 per mmbtu. The record also suggests that these differentials are the proximate result of different dates of contracting and rapidly changing market conditions, both of which will ordinarily be considered rational bases for differences in price interference with which is beyond the Board's authority.

Transco, required to take ratably by Rule 48, is free to offer owners having no contract a price reasonable in the context of the then existing market conditions. If the owner thinks the price is too low and wishes to risk drainage, he does not have to sell. But he has no legal redress simply because he failed to lock in a price via contract at a time when the market was more favorable.

The owners of interests in a common source of supply are perfectly free to contract for the sale of their share of production on whatever terms they can negotiate. If owners such as Coastal desire to operate without a contract, for whatever reason, this is their privilege. If there should be an overall market shortage and increased demand amongst consumers, parties such as Coastal certainly stand to benefit. On the other

hand, where a market glut and decreased demand occur, Coastal and others no doubt suffer.

Why in an era of deregulation freedom of contract is perceived to be bad as a matter of policy escapes us. The national policy, to be sure not a preemptive one, is that the price of natural gas at the wellhead shall be regulated by market and geological forces, not judicial or administrative fiat. Regulation as heretofore practiced has failed. Whatever bugs may remain in the "deregulation system" and whatever fine tuning may be needed in our laws, the efficacy of regulation remains questionable and its substantial costs demonstrable. Pierce, *Reconsidering The Roles of Regulation And Competition In The Natural Gas Industry*, 97 Harv.L.Rev. 345, 371-372 (1983). The ultimate regulator of the price of such gas, at least for the moment, is what the consumer is willing to pay, with FERC interjecting itself into the picture only where wellhead prices have been set by fraud or collusion.

A caveat need be added: we do not hold that a pipeline purchaser may offer any terms, take-it-or-leave-it, and meet its Rule 48 obligations. Offering a working interest owner a choice between a substantially below market price or otherwise wholly unreasonable terms, on the one hand, and drainage, on the other, is simply not a ratable taking and is a violation of Rule 48. To comply with its Rule 48 obligations the pipeline must offer in good faith reasonable terms, including a reasonable price, determined by reference to prevailing market conditions and other appropriate economic considerations.

Of course, nothing in Rule 48 requires that Transco take any gas from a given source of supply. If it takes at all, however, it must take, or in good faith offer to take ratably.

So much of Order No. 409-82 as may be construed to require that Transco, in the course of performing its lawful duty to take ratably, pay Coastal and others not under contract $7.907 per mmbtu is reversed.

G. Miscellaneous Other Alleged Errors in Board Rulings

Transco presents to the Court further assignments of error, denominated in its brief, Reversible Errors In The Board's Rulings.

First, Transco argues that the Board was arbitrary and capricious in finding that Transco was discriminating against Coastal and owners of relatively small working interests in violation of Rule 48. We made clear above in Section II(C) entitled "Non-Facts" that neither the "size" of the parties nor of their interests was a fact of legal significance here. Nothing said in the intervening pages should cause us to lose sight of that elementary proposition.

In any event, our substantive holding that Transco has lawfully been ordered to take ratably (if it takes at all) and to take ratably the gas of each owner in the common pool without regard to size of owner or interest coupled with our further holding that the Board has no authority to engage in price regulation should effectively dispose of this issue.

Next, Transco argues that there is no substantial evidence to support the Board finding that ratable production occurred prior to July 1, 1982, and that Transco's "cutback" has or will cause non-ratable withdrawals or drainage. The point is specious. There may well be reasons not attributable to Transco why there may not have been ratable production prior to July 1, 1982. This would do nothing to ameliorate the undeniably discriminating effect of Transco's refusal after July 1, 1982, to take ratably, and more specifically, to take the production of the non-contract interest owners. The assignment of error is rejected.

Finally, Transco argues that the Board improperly refused to receive and consider relevant evidence proffered by Transco and other parties to the substantial prejudice of Transco. We find no merit in this contention.

The hearing of this matter was had in accordance with the official Rules Of Order And Procedure For Hearings Before The Board, Order No. 201-51, Rule 13(c) of which provides

> (c) The materiality, relevancy and competency of any testimony shall be subject to challenge by any party to the hearing or by any member of the Board. When so interposed, such objections shall be acted upon by the Chairman or by the Acting Chairman, his ruling thereon being subject to change by a majority vote of the Board members then sitting.

There is no necessity for enumeration of the points recited by Transco here. Suffice it to say that Transco has not suffered cognizable prejudice from any of the Board's evidentiary rulings, in that none of the excluded evidence would have proved or tended to prove that after July 1, 1982, Transco was taking ratably. Absent prejudice, any error in exclusion is harmless and cannot be grounds for reversal. *Planters Bank v. Garrott*, 239 Miss. 248, 270, 122 So.2d 256, 264 (1960). All other assignments of error not heretofore expressly passed upon are denied and rejected.

IV. CONCLUSION

For the reasons set forth above, so much of Order 409-82, and the Circuit Court's affirmance thereof, as requires that Transco, if it takes or purchases natural gas from the Harper Sand Gas Pool in Greens Creek and East Morgantown Fields, take ratably from the common pool and without discrimination in quantity or percentage thereof in favor of one owner, operator or producer against another in such common pool is affirmed.

So much of Order 409-82, and the Circuit Court's affirmance thereof, as may be construed to require that Transco, if it takes or purchases from said pool, purchase without discrimination in price is reversed and rendered.

This matter is remanded to the Circuit Court with instructions that the matter be further remanded to the State Oil and

Gas Board for such further proceedings as may be appropriate not inconsistent with this opinion.

Taxable costs in this Court, before the Circuit Court, and before the Board shall be and they hereby are taxed one-half against Transco as Appellant and one-half against Appellees, jointly and severally, for all of which let execution issue.

AFFIRMED IN PART; REVERSED IN PART.
WALKER, P.J., ROY NOBLE LEE, P.J., DAN M. LEE, PRATHER, AND SULLIVAN, JJ., CONCUR. PATTERSON, C.J., BOWLING, HAWKINS, JJ., NOT PARTICIPATING.

APPENDIX B

IN THE CIRCUIT COURT OF THE FIRST JUDICIAL DISTRICT OF HINDS COUNTY, MISSISSIPPI

No. 29,393

TRANSCONTINENTAL GAS PIPELINE CORPORATION
Appellant

VS.

THE STATE OIL & GAS BOARD OF MISSISSIPPI, COASTAL EXPLORATION, INC., WILEY FAIRCHILD, RODNEY FAIRCHILD, W. R. FAIRCHILD CONSTRUCTION COMPANY, AND INEXCO OIL COMPANY
Appellees

COASTAL EXPLORATION, INC.
Appellee
and Cross-Appellant

VS.

TRANSCONTINENTAL GAS PIPELINE CORPORATION, GETTY OIL COMPANY, TOMLINSON INTERESTS, INC., AND THE STATE OIL & GAS BOARD OF MISSISSIPPI

Appeal From The State Oil And Gas Board of Mississippi

MEMORANDUM OPINION AND ORDER OF THE COURT

This case is before the Court as an appeal by Transcontinental Gas Pipeline Corporation ("Transco") from Order No. 409-82 entered by the State Oil and Gas Board of Mississippi ("Board") in a contested matter in which Transco was the respondent. The Board found that Transco was violating the Board's Statewide Rule 48 by engaging in discriminatory purchasing practices among producers in a gas pool, and was violating Mississippi Code Annotated Section 53-3-3 and 53-3-1 by committing and causing "waste" to take place by Transco's unratable takes of gas from wells producing from the gas pool so as to cause unit-to-unit drainage. Among other things, the Board ordered Transco to purchase without discriminating against certain producers and to take gas ratably from the wells producing from the gas pool, if and when Transco took gas from the pool.

Transco's assignments of error fall into three (3) general categories:

(1) Claimed procedural and evidentiary errors by the Board (assignments 1 through 3);

(2) The claimed lack of jurisdiction or authority under state law to adopt or enforce Statewide Rule 48 (assignments 4 and 5); and

(3) Federal claim challenges which, in substance, allege that Statewide Rule 48 and Order No. 409-82 attempt to regulate an area which has been preempted by federal law, and are unconstitutional. (assignments 6 through 9)

As to Transco's federal claim challenges, Transco has assigned these alleged errors but has also attempted to "reserve" these issues for litigation in federal court, relying on *England v. Louisiana State Board of Medical Examiners*, 375 U.S. 411 (1964), as authority. Coastal Exploration, Inc. ("Coastal") has

filed a Motion to Strike Attempted Reservation of Federal Claims, with supporting exhibits, asking the Court to strike the attempted reservation and rule on all of the assigned errors.

The Court affirms Order No. 409-82 in its entirety and, in so doing, sustains Coastal's Motion to Strike Attempted Reservation of Federal Claims, disregards the attempted reservation of the assigned errors, and addresses all of the assigned errors. In doing so, the Court is mindful of and takes judicial notice of the fact that the state law and federal law issues before this Court are of extremely important interest to all facets of the oil and gas industry of this state, as well as the other oil and gas producing states of this country, concern vital state interests, and need and deserve an early and complete resolution in the forum in which they arose.

There can be no meaningful discussion of these important issues without a review of the facts which the Court finds to have been established by the evidence before the Board. Thus, it is appropriate first to review just how this controversy developed. How did the parties get here from there?

FACTS

The Harper Sand Gas Pool underlies portions of both the Greens Creek Field and the East Morgantown Field of Marion County, Mississippi. These two field are contiguous. If only one well were completed into this pool and produced from this pool, it would drain the entire pool.

Six gas wells are completed into and producing from the Harper Sand Gas Pool: The Getty-Rogers 28-11 Well, the Getty-Sipp 20-9 Well, the Tomlinson-Willoughby 3-5 Well, the Getty-Buckley 33-6 Well, The Florida Exploration-Carlisle 4-2 Well and the Florida Exploration-Barnes 29-1 Well. The Harper Sand Gas Pool produced by these wells lies below 15,000 feet and all of the wells producing from this pool have

been classified as "deep, high-cost wells" under Section 107(c) of the Natural Gas Policy Act of 1978 ("NGPA").

Coastal owns small undivided working interests (generally less than 1%) in the units for four of the six wells which produce from this pool, owning in the Rogers, Sipp, Willoughby and Barnes wells. Coastal participated in the drilling of each of these wells, voluntarily paid its share of drilling and completion costs, and has timely and regularly paid its share of operating costs for each of these wells. Because of its ownership in these wells, Coastal owns and has the right to its fair and equitable share of gas produced from the pool by the wells.

When the wells in question first began producing gas in April 1981, with production from the Sipp Well, the gas was sold to Transco. Getty, as the operator and owner of a substantial working interest in the Getty-operated units, had previously entered into a gas purchase contract with Transco. Transco had not negotiated or offered gas purchase contracts to each of the many other working interest owners in the Getty-operated wells, so that many owners of small undivided interests, like Coastal, had no gas purchase contract when first production began. However, in accordance with the industry practice, Getty produced all owners' gas and delivered the gas to Transco which in turn purchased and paid for all of the gas at the same price and on the same terms and conditions as Transco purchased and paid for Getty's share of gas. This practice was consistent with Statewide Rule 48, which forbids purchasers from discriminating in favor of one owner, operator or producer against another in the same common source of supply.[1]

As the other wells completed into the pool began producing, the same procedure was followed, the effect being that Transco

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[1]Statewide Rule 48 of the State Oil and Gas Board provides as follows:

"Each person now or hereafter engaged in the business of purchasing oil or gas from owners, operators, or producers shall purchase without discrimination in favor of one owner, operator or producer against another in the same common source of supply."

took gas ratably as between the wells producing from the pool and purchased gas without discrimination in favor of the operator as against Coastal and the other owners of small undivided interests.

This situation continued from April 1981 until on or about July 1, 1982, when Transco ceased purchasing the gas of owners (producers) who did not have a contract with Transco. In May 1982, Transco notified Getty and Tomlinson that effective June 1, 1982 (later changed to July 1, 1982), Transco would no longer take or purchase the gas of those producers who had not entered into a gas purchase contract with Transco, so-called "non-contract producers." However, because of certain provisions of the Florida-Transco gas contract, Transco would continue to purchase non-contract producers' gas produced from the Florida-operated wells and pay those producers the same price Transco paid Florida.

After receiving this notice from Transco, Getty and Tomlinson notified Coastal that they, as operators, would not produce Coastal's share of gas from the Rogers, Sipp and Willoughby Wells unless Coastal obtained its own purchaser and its own gas purchase contract. A similar type notice was sent to other non-contract producers.

On or about July 1, 1982, production of the Rogers, Sipp and Willoughby wells was reduced or cut-back to account for Transco's refusal to buy non-contract producers' gas from those wells. The result was that Transco began taking gas unratably from the wells producing from the pool, taking a lesser percentage of deliverability from the Getty and Tomlinson Wells than from the Florida Wells.

Following the notice from Getty and Tomlinson, Coastal attempted to obtain another gas purchaser to whom it could sell its gas, but was unsuccessful. Coastal then requested Transco to purchase Coastal's share of gas producible from the Rogers, Sipp and Willoughby Wells on the same terms and conditions as Transco purchased gas from the operators of those wells or to give Coastal a gas purchase contract like

Transco had given the operators. However, at that point in time Transco refused to purchase Coastal's gas at all.

On July 29, 1982, Coastal filed a petition with the State Oil & Gas Board to require Transco to comply with Statewide Rule 48 by ratably taking gas from the wells producing from the common pool and purchasing without discrimination in favor of the operators, Getty and Tomlinson, against Coastal. After Coastal filed its petition, Transco then offered to buy Coastal's gas at $5.00 per MMBTU under a contract which would contain a "market out" clause to allow Transco to lower the contract price whenever Transco felt that the price was "uneconomic." Transco's gas purchase contracts with Florida, Getty and Tomlinson contained no such clause, and Transco planned to continue paying Getty and Tomlinson $7.90 per MMBTU for their share of gas produced from the same wells. Coastal did not accept this proposal, claiming that it violated Statewide Rule 48.

At the hearing before the Board in September 1982, Transco claimed that Statewide Rule 48 was invalid as a matter of state law and that the Board had no authority to require Transco to ratably take or purchase without discrimination because federal law had allegedly preempted the area, and because Rule 48 allegedly was unconstitutional for a variety of reasons.

A three day trial was held before the Board during which Transco defended the action by the presentation of witnesses, exhibits and legal arguments, raising as defenses the same claims which it now asserting before this Court.

The Board granted Coastal's petition and on October 13, 1982, entered its Order No. 409-82 dated September 16, 1982. On October 15, 1982, Transco perfected its appeal to this Court.

THE ASSIGNMENTS OF ERROR

The Court chooses to address the Assignments of Error in the reverse order in which they are raised because the claims of federal preemption and unconstitutionality of the Board's ac-

tion are the threshold issues. If the Board's order has invaded an area preempted by the federal government or is unconstitutional, then there is no need to reach and decide the issues of state authority and substantial evidence. However, in order to reach the claims of federal preemption and unconstitutionality, the Court must first consider the claimed *England* reservation.

THE CLAIMED ENGLAND RESERVATION

Before considering the propriety of the claimed *England* reservation, it is appropriate to review the facts relevant to the claimed reservation.

In response to Coastal's petition filed with the Board, Transco raised several federal claim defenses and objections to the subject matter jurisdiction of the Board, Transco's contentions being that (1) the owner of the Board to issue such an order had been preempted by the Federal Energy Regulatory Commission's ("FERC") jurisdiction under the Natural Gas Act ("NGA") and the NGPA, (2) that Statewide Rule 48 violated the Commerce Clause and (3) that the requested relief would be discriminatory against Transco (presumably an equal protection argument), would constitute an unlawful taking of private property without compensation (presumably a due process argument) and would impair Transco's right to contract (presumably a Contract Clause argument). Before the Board hearing was held, the Board specifically requested and received briefs from the parties, including Transco, on the federal preemption claims. However, the Board rejected all of Transco's federal claim defenses, concluding that the Board had subject jurisdiction of the controversy.

On October 13, 1982, the day the Board actually entered Order No. 409-82, Transco filed suit in the United States District Court for the Southern District of Mississippi naming the State Oil and Gas Board as a Defendant and asserting as its federal claims the very same federal claim defenses which it had raised in the state proceedings before the Board. Coastal,

Getty and Tomlinson subsequently intervened in that federal suit on the side of the Board.

Assignments of Error 6 through 9 are the same federal claim defenses which Transco raised and litigated in the proceedings before the Board. However, Transco claims that *England* allows it to assign these items as errors before this Court, yet reserve them for determination in the federal suit it filed after the conclusion of the state trial proceedings.

Transco's reliance on *England* is misplaced. This is because *England*, by its own terms as well as by the cases which have applied it, applies only when the following conditions are met.

1. First, suit is filed in federal district court in the first instance.

2. Second, the federal district court then abstains from the exercise of its jurisdiction, pursuant to *Railroad Commission of Texas v. Pullman Company*, 312 U.S. 496, 61 S.Ct. 643 (1941) ("Pullman Abstention"), pending a determination of a question of unsettled state law.

3. Third, the federal plaintiff is then relegated to state court in order to get a determination from the state court regarding the question of unsettled state law.

4. Fourth, the federal plaintiff, who has been ordered into state court against its will, whether as a plaintiff or defendant in the state court action, may then "reserve" its federal claims from being decided in the state court suit so that, at the conclusion of the state court suit, the federal plaintiff may return to federal court for a determination of its federal claims originally asserted in federal court.

These conditions for an effective *England* reservation have not been met in the case at hand. Transco initiated its federal court suit on October 13, 1982, on the same day as the Board entered its order concluding those proceedings, almost three (3) months after Coastal commenced the proceedings before

the Board which are the subject of this appeal. With regard to the second condition set forth above, the Court notes that on February 18, 1983 the Federal District Court for the Southern District of Mississippi entered its "Memorandum Opinion" declining to abstain from the exercise of its jurisdiction on the grounds that it was inappropriate because, *inter alia*, "Statewide Rule 48 appears to be settled." Under *England*, it is only in the event that Pullman Abstention is ordered by a district court that a federal plaintiff, who is then sent to state court against his will, may "reserve" his federal claims for later determination in federal court after he returns there from state court. In this case, however, the federal district court has retained its jurisdiction and has not ordered Pullman Abstention.

An examination of the cases which have applied *England* reveals that it does not stand for the proposition that a litigant (like Transco) has the right to raise federal claim defenses as a defendant in a state proceeding and then, after losing at trial, assign them as grounds for reversal of the state action but "reserve" those alleged errors for "determination" in federal court without pursuing them on appeal through the state courts. Among other defects in that procedure is the fact that it represents an attempt to appeal from a state administrative agency or court to federal court. An *England* reservation is available only where the controversy initially arises by way of a federal court suit which is filed before state proceedings are initiated, followed by the federal court then abstaining under *Pullman* and relegating the federal plaintiff to state court to resolve alleged "unsettled" questions of state law. In particular, see, e.g., *Gresham Park Community Organization v. Howell*, 6S2 F.2d 1227, 1243 (5th Cir. 1981), *Cornwell v. Ferguson*, 546 F.2d 1022 (5th Cir. 1977), and *Ball v. Board of Trustees*, 584 F.2d 684 (5th Cir. 1978), which stand for the proposition that an *England* reservation is not available where the controversy first began in state court or before a state administrative agency; and *Fair Assessment v. McNeary*, 454 U.S. 100 (1981), *Roy v. Jones*, 484 F.2d 96 (3rd Cir. 1973), *Howell v. State Bar of*

Texas, 674 F.2d 1027 (5th Cir. 1982) and *Allen v. McCurry*, 449 U.S. 90 (1980), holding that Pullman Abstention must be ordered by the federal district court in order for an *England* reservation to be available in state court; and *Harman v. Forssenius*, 380 U.S. 528 (1965), and *Alt v. City of Biloxi*, 397 So.2d 897 (Miss. 1981), which stand for the proposition that an *England* reservation is not available unless Pullman Abstention is ordered because of an unsettled question of state law.

In the words of the Mississippi Supreme Court in *Alt v. City of Biloxi*, *supra*, which case considered an *England* reservation question, Transco, as the respondent or defendant to the Board proceedings, "is not a party who had 'a choice' between state and federal courts and who chose the latter."

Accordingly, the Court sustains the Motion to Strike Attempted Reservation of Federal Claims, disregards the attempted reservation, and considers the federal claim challenges which have been assigned by Transco as errors.

I. FEDERAL CLAIM CHALLENGES

1. The Federal Preemption Claim

In its Assignments of Error and in its defenses before the Board, Transco has claimed that the Board's authority to regulate or affect an interstate gas pipeline's purchase of natural gas has been preempted by the Natural Gas Act of 1938 (NGA) and the Natural Gas Policy Act of 1978 (NGPA) and is within the exclusive jurisdiction of the Federal Energy Regulatory Commission (FERC), the successor to the Federal Power Commission (FPC). Transco places principal reliance upon *Northern Natural Gas Company v. Corporation Commission of Kansas*, 372 U.S. 84 (1963), wherein the Supreme Court held invalid a ratable take/minimum price order entered against an interstate pipeline because, at that point in time, the order invaded the FPC's regulatory jurisdiction under Section 1(b) of the NGA. However, Coastal et al contend that the effect of the passage of the NGPA in 1978, and specifically NGPA Section

601(a), has been to exempt the "first sale" of the type of gas produced from the Harper Sand Gas Pool, from the NGA and FERC's jurisdiction under that Act. If Coastal is correct in its contention,then *Northern Natural*, and the NGA jurisdiction concerns which prompted that decision, is not applicable here, and the Board's order can be upheld as a matter of federal and constitutional law under *Cities Service Gas Company v. Peerless Oil & Gas Company*, 340 U.S. 179 (1950), in which the Supreme Court upheld a ratable take order similar to Order No. 409-82. The issues thus drawn, a brief review of both the NGA and NGPA are in order, particularly the reasons prompting passage of the NGPA in 1978.

The Natural Gas Act of 1938 and the Natural Gas Policy Act of 1978

Section 1(b) of the NGA, 15 U.S.C.A. Section 717(b), is the jurisdictional section of the Act and clearly defines the scope of the NGA, to-wit:

> The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

In 1947, the United States Supreme Court, in *Panhandle Eastern Pipeline Company v. Public Service Commission of Indiana*, 332 U.S. 507, 92 L.Ed. 128, 68 S.Ct. 190 (1947), examined Section 1(b) of the NGA and defined the powers granted to the FPC:

> This section [Section 1(b)] determines the Act's coverage and does so in the light of the situation existing at the time. Three things and three only Congress drew within

> its regulatory power, delegated by the act to its agent, the Federal Power Commission. These were: (1) the transportation of natural gas in interstate commerce; (2) its sale in interstate commerce for resale; and (3) natural gas companies engaged in such transportation or sale. (332 U.S. at 516).

This statement was quoted with approval in *Federal Power Commission v. Louisiana Power & Light Company*, 406 U.S. 621, 32 L.Ed. 2d 369, 92 S.Ct. 1827 (1972). Based upon the language of the NGA itself, as well as the above-mentioned cases, it is clear that FERC's jurisdiction, although wide ranging, is less than plenary. FERC's grant of jurisdiction flows from Section 1(b) of the NGA. It can regulate the activities of producers and pipelines only insofar as it is permitted to do so by the Act.

Prior to enactment of the NGPA in 1978, two NGA regulatory features actively discouraged the introduction of new supplies of natural gas into interstate commerce: (1) the literal regulatory maze which a producer and a pipeline had to go through and comply with before a pipeline could purchase gas for the interstate market, and (2) extremely low NGA-mandated and FERC determined "just and reasonable" ceiling prices which a pipeline could pay a producer for gas.[2]

The extent of FERC's pre-NGPA total control over all aspects of the producer/pipeline sale and purchase of gas can be appreciated by an examination of FERC's pre-NGPA/NGA-power to grant or deny a certificate of public convenience and necessity. Under the NGA, gas could not even lawfully enter the interstate market unless FERC first issued a certificate of public convenience and necessity. FERC would not issue the required certificate unless the producer-pipeline contract contained certain price limitation clauses and excluded other types

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[2]*See* e.g., analysis of the NGA set forth in *Tenneco, Inc. v. Sutton*, 530 F. Supp. 411, at 417–18 (M.D. La. 1981).

of clauses.[3] Thus, through its power to grant or deny the required certificate of public convenience and necessity, FERC was able to directly dictate the contract terms and price which a pipeline could pay and a producer could receive.

The reason the ratable take order in *Northern Natural* invaded the FPC's jurisdiction under Section 1(b) of the NGA was because the order, at *that* point in time, directly conflicted with two of FPC's then fundamental regulatory powers: FPC's NGA power to admit or deny the entry of gas into interstate commerce, and FPC's NGA power of approval (or disapproval) of the price paid for the gas by the pipeline. The Kansas ratable take order at issue in *Northern Natural* clearly interferred with both of those two powers because (1) the order forced gas into interstate commerce without a *then* required certificate of public convenience and necessity from FPC, and (2) the order required the payment of a set price without the *then* require prior adjudication by FPC that the price was "just and reasonable." As hereinafter discussed, neither of those two regulatory powers survived enactment of the NGPA as to "undedicated gas"[4] or Section 107 gas[5] or "dedicated gas" which is also qualified as NGPA Section 102 or 103 gas.

It was because of these discouraging features of the NGA and FERC's regulatory powers under the NGA that producers began selling their gas in the *intrastate market* (they did not have to deal with the NGA or FERC and they could get a much higher unregulated price), and concomitantly, pipelines like Transco were unable to purchase gas for the *interstate market*. By the late 1970s this "cause and effect" finally culminated in severe gas shortages in the interstate market, while at the same time there existed an abundance of higher priced gas in

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[3]*See*, e.g., 18 C.F.R. Sections 154.93 and 154.103. *See also* the "Curtis/Jackson Letter" of September 8, 1978 which appears as a part of the legislative history of the NGPA.

[4]"Undedicated Gas" is gas which was not committed or dedicated to interstate commerce as of November 8, 1978. *See* NGPA Section 601(a)(1)(A).

[5]*See*, NGPA Section 601(a)(1)(A)(B).

the intrastate market. That "national problem" of gas shortages in the interstate market was *the* fundamental reason why Congress passed the NGPA.[6]

In passing the NGPA, Congress had two central goals: To provide price incentives to producers to drill more wells, find new gas and put that new gas into the interstate market, and to free the producers and pipelines from those regulatory aspects of the NGA and FERC's jurisdictionwhich were discouraging producers from selling gas to the pipelines and crippling pipelines' ability to purchase new gas.[7]

Those congressional goals were reached by Congress (1) eliminating FERC's NGA-jurisdiction and power to require a producer and a pipeline to obtain FERC approval of the entry of new gas into the interstate market and FERC approval of the price to be paid by the pipeline for that gas, and (2) enacting immediate price deregulation for some new gas (like "deep, high-cost gas" under Section 107), and gradual price deregulation for other new gas (like gas under Sections 102 and 103). Sections 121 and 601 of the NGPA accomplished these goals.

First, Section 121 was included to provide producers with the price incentives they needed to find new gas and sell that gas in the interstate market. Thus, Section 121 immediately eliminated price controls for Section 107 "deep, high-cost gas" and set a 1985 date for price deregulation of other new gas, such as gas qualifying for pricing under Sections 102 and 103. Section 121 thus furnished the price incentives which Congress intended.

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[6]*See*, e.g., *Tennecco, Inc. v. Sutton, supra*, 530 F.Supp. at 418, n. 24 and 25 at 420–21; *Mid-Louisiana Gas Co. v. FERC*, 664 F.2d 530, 533 (5th Cir. 1982); *Pennzoil Co. v. FERC*, 645 F.2d 360, 380 (5th Cir. 1981), at 367, n. 13.

[7]*See*, e.g., authorities cited in note 6, *infra*. *See also Pennzoil Co. v. FERC, supra*, 645 F.2d at 378 ("The NGPA is a fundamental change in regulatory outlook.") In *Pennzoil*, the court concluded that the effect of § 601(a)(1)(A) was to deny FERC the authority to regulate or interpret gas purchase contracts covering "undedicated" gas. *Id* at 380. *See also Mid-Louisiana Gas Co. v. FERC, supra* 664 F.2d at 535.

Second, Section 601 was included to provide producers and pipelines with freedom from regulatory interference by FERC with the pipelines' purchase and the producers' sale of new gas; to enable the pipelines to freely compete with unregulated contractual terms to buy new gas by allowing the pipelines to pay the producers the higher incentive prices for new gas (without *ever* having to get FERC approval of the prices paid or the other terms of the contract); and to exempt the pipelines and producers alike from the then existing constraints of the NGA and FERC's regulatory jurisdiction under the NGA, constraints which had combined with the low FERC-set "just and reasonable" prices (based on cost of service) to produce the severe gas shortages of the late 1970s brought on by the producers' reluctance (and sometimes refusal) to sell their gas in interstate commerce, and the pipeline's inability to buy new gas from the producers. Section 601 thus furnished the pipelines and the producers the degree of freedom from regulatory interference from FERC which Congress intended.[8]

Analysis of Section 601

Under the Section 601 statutory scheme, Section 601(a)(1) removes FERC's NGA-jurisdiction to directly or indirectly control or regulate a pipeline's purchase of Section 107 gas and the price paid by the pipeline for that gas. In place of that "lost" jurisdiction over the pipeline's purchases of that gas, Section 601(c) gives FERC the jurisdiction and power to deny a

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[8]*See*, e.g., *Tenneco, Inc. v. Sutton*, *supra*, 530 F.Supp. at 419: "These provisions [Section 601] remove the Commission's authority to establish just and reasonable prices under the NGA for producer sales into the interstate market and to indirectly regulate these sales through control of the interstate pipeline purchaser's pass-through of purchase gas costs."

See also the "Curtis/Jackson Letter", *supra*, on Section 601: "This section [601] executes the legislature intent to remove from Natural Gas Act utility type regulation natural gas not heretofore dedicated or committed to interstate commerce (§ 601(a)(1)(A), and to remove from Natural Gas Act-type regulation heretofore jurisdictional sales of high cost gas, gas from new OCS leases, new well qualifying for the new natural gas price under section 102, and [103 gas] (§ 601(a)(1)(B))." FPAS § 601: 220, page 2.

pipeline a pass-through of the price the pipeline pays for 107 gas, but *only* if FERC can prove that the price results from "fraud, abuse or similar grounds." Moreover, FERC's power to deny a pipeline a pass-through can be exercised *only* against the pipeline and *only* when (and if) the pipeline comes before FERC to obtain authority to pass-through the entire price paid by the pipeline and include that price in the resale rates charged by the pipeline to consumers. However, FERC still has no authority or jurisdiction (not even under Section 601(c)) to regulate or control a pipeline's purchase of 107 gas, or the price the pipeline pays to producers or the pipeline's contract with the producers.

The Court's inquiry into the preemption claims raised by Transco merits a brief sub-section by sub-section analysis of just how Congress used Section 601 to free the producers and pipelines from the NGA and FERC's NGA-jurisdiction to control purchases and sales of 107 gas, contract terms and prices paid by pipelines for 107 gas. This analysis is relevant to the claim that *Northern Natural* applies in this case.

First, Congress included Section 601(a)(1) to eliminate the NGA requirement that the parties had to first obtain from FERC a certificate of public convenience and necessity as to new gas, and to remove FERC's jurisdiction and power to set a "just and reasonable" price and dictate contract terms. Section 601(a)(1) provides that the first sale of undedicated gas is never made subject to the NGA or FERC's NGA-jurisdiction.[9] The *effect* of this particular sub-section is that neither the producer nor the pipeline ever has to obtain the previously required certificate of public convenience and necessity in order to sell

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[9]NGAP § 601(a)(1)(A)&(B); Joint Explanatory Statement of the Committee on Conference of the House and Senate. *Accord, Pennzoil Co. v. FERC*, 645 F.2d at 380.

and buy this type of new gas.[10] Because the parties do not have to obtain a certificate from FERC, FERC cannot use its NGA power (to grant or deny a certificate) to control purchases, contract terms and price, as it did prior to enactment of the NGPA and at the time *Northern Natural* was decided.[11] Nor can FERC, pursuant to its NGA jurisdiction over a "natural gas company," control the price which a pipeline like Transco pays for the gas on the grounds that Transco is an otherwise regulated "natural gas company." Section 601(a)(1)(D) provides that Transco shall not be considered to be a "natural gas company" with respect to its purchase of Section 107 gas.

Second, Congress included Section 601(b) and (c) to protect a pipeline from an after-the-purchase attack by FERC on the price which the pipeline pays for Section 107 gas. Section 601(b) provides that all prices which the pipeline pays for Section 107 gas are deemed "just and reasonable" as a matter of law, and Section 601(c) provides that the pipeline has the guaranteed statutory right to pass-through the price which it pays

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[10]*See*, e.g., *Conoco, Inc. v. FERC*, 662 F.2d 796, 797, 799 (5th Cir. 1980). *See also* FERC's Preamble to the issuance of the first interim regulations issued after the NGPA was passed, 43 F.R. 56448 (12-1-78), wherein FERC observed the effect of the NGPA on the NGA:

> "If gas is not committed or dedicated to interstate commerce . . . or is exempted from the jurisdiction of the NGA under section 601(a)(1)(B) as [107 or 102 or 103 gas] the prior framework of utility-type regulation under the NGA no longer applies.
>
> If natural gas sales are freed from the requirements of the NGA, several adjustments to NGA regulation are obviated. First, there is no longer any necessity for a producer to seek certification of the sales as serving the public convenience and necessity." *Id.*

[11]*See*, e.g., *Pennzoil Co. v. FERC*, *supra*, in which the Fifth Circuit held that FERC no longer has jurisdiction to regulate or interpret gas purchase contracts covering undedicated gas or dedicated gas which is also 107 or 102 or 103 gas: "In other words, section 601(a)(1)(A) prevents the universe of gas subject to the NGA from expanding." 645 F.2d at 380.

for Section 107 gas and include that price in its resale rates charged to consumers.[12]

A pipeline can be denied its guaranteed statutory right to pass-through the price paid to producers *only* if FERC finds that the price results from "fraud, abuse or similar grounds." *See* Section 601(c)(2). That particular determination can be made *only* in rate proceedings before FERC in which the pipeline seeks authority to pass-through the Section 107 price and include that price in its resale rates to consumers. FERC can deny the pipeline a pass-through of *only* that portion of the Section 107 price which results from "fraud, abuse or similar grounds." However, FERC still has no jurisdiction or authority to prevent the pipeline from purchasing 107 gas or paying deregulated prices to the producer, as it could at the time *Northern Natural* was decided.

Thus, under Section 601(a)(1) (A) and (B) the entire first sale transaction of new gas is removed from the NGA and FERC's NGA-jurisdiction, and, to drive home the point, Section 601(a)(1)(D) further removes the former NGA-jurisdiction given FERC by NGA Section 2(b) by declaring that the pipeline purchaser is *not* a "natural gas company" with respect to its purchase of new gas. Because a "first sale" means the *entire* first sale transaction (both the producer's "sale" and the pipeline's "purchase"), neither the producer nor the pipeline is subject to FERC's NGA-jurisdiction with respect to a first sale of this gas. The practical effect of Section 601(a) (1) is that FERC cannot prevent, regulate or control a pipeline's purchases and takes of Section 107 gas nor the price which the pipeline pays for that gas; FERC cannot directly or indirectly regulate, control or dictate the contractual terms on which the gas is to be sold and purchased; the pipeline and the producers do not ever have to obtain FERC's approval of the price paid by the pipeline; and the pipeline and the producers do not ever

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[12]*See*, e.g., *Pennzoil Co. v. FERC*, 645 F.2d 360, 379 (5th Cir.): "Section 601(c)(2) guarantees to interstate pipelines the ability to pass through NGPA payments."

have to obtain a certificate of public convenience and necessity from FERC in order for the pipeline to be able to buy the gas and bring it into the interstate market. Needless to say, this is a vastly different regulatory scheme from that which was in existence under the NGA when *Northern Natural* was decided.

As it relates to the Rule 48 issue now before the Court, because the NGPA now exempts the first sale of 107 gas from the NGA and FERC's NGA-jurisdiction, then Statewide Rule 48 and Order No. 409-82, which apply to only the wellhead "first sale" of 107 gas, do not conflict with, invade, nor infringe upon FERC's NGA-jurisdiction. The NGA-jurisdictional reasons why the Supreme Court voided the ratable take order in *Northern Natural* no longer exist as to Section 107 gas. As to 107 gas, the State is therefore free to re-enter the limited area which it was allowed to regulate under *Cities Service Gas Co. v. Peerless. supra.*

Thus, the Court concludes that Statewide Rule 48 and Order No. 409-82 do not regulate or invade areas or matters which have been preempted by the NGA or the NGPA.

2. The Commerce Clause, Due Process Clause and Equal Protection Clause Claims

The constitutionality of a ratable take/minimum price order similar to Order No. 409-82 was upheld in *Cities Service Gas Company v. Peerless Oil & Gas Company,* 340 U.S. 179 (1950), a case in which the Supreme Court rejected the same type of due process, equal protection and commerce clause arguments which Transco has assigned as errors. The plaintiff in *Peerless* found itself in somewhat the same factual situation as Coastal. There, Peerless had no pipeline outlet of its own and was being drained by production from offsetting wells from which Cities Service, an interstate pipeline company, was purchasing gas. Peerless offered to sell the gas from its wells to Cities Service but Cities Service refused to take the gas unless Peerless would dedicate all of its gas at a price which was lower than that being paid to other owners in the field. The Oklahoma Corpora-

tion Commission ordered Cities Service to purchase gas from Peerless ratably and at not less than a minimum price which was fixed by the Commission. On appeal, first to the state courts and then to the Supreme Court, Cities Service claimed that the state could not engage in "price fixing" and that the ratable take order violated the due process, equal protection and commerce clauses. The Supreme Court upheld the ratable take/minimum price order and rejected all of Cities Service's constitutional claims. *Id.* 340 U.S. at 185-188, 71 S.Ct. at 219. Only recently, the Supreme Court cited *Peerless* for the proposition that the states have the power to regulate natural gas prices and sales as long as that regulation does not interfer with interstate commerce. *See, Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 103 S.Ct. 697 (1983), an NGPA case.

One of Transco's principal constitutional arguments is that Rule 48 and Order No. 409-82 are unconstitutionally vague. This vagueness claim was not raised by Transco at trial. Although ratable take statutes, rules, and orders are seldom construed by appellate courts, the applicable case law and the facts refute Transco's assertion that Rule 48 and Order No. 409-82 are unconstitutionally vague. The decisions indicate that the task of compliance with a ratable take order can be worked out between the state entity issuing the order and pipeline to whom it is directed.

In *Railroad Commission v. Rio Grande Valley Gas Company*, 405 S.W. 2d 304 (Tex. 1966), Rio Grande asserted that an order of the Texas Railroad Commission, issued pursuant to the Texas Common Purchaser Act, requiring Rio Grande to extend its gathering line to a particular well and to "connect said well and to take gas therefrom without unjust or unreasonable discrimination in favor of its own [Rio Grande's] production or that of any other producer in said field area and without unjust or unreasonable discrimination," was fatally defective because it did not with sufficient certainty inform Rio Grande as to the price it was to pay for the gas in question or as to the quantity of gas Rio Grande was to take from the well. The

Texas Supreme Court upheld the validity of the order, noting that "the provisions of the order follow the statute. Neither price nor quantity of take are prescribed. This does not mean that such factors may not be ascertained." (*Id.* at 311).

The Texas Supreme Court also made the following observations:

> Ordinarily, the question of price is one to be settled by agreement of the parties, and it is not the function of the Commission primarily to set a well head price per MCF. The same may also be said as to the amount of gas to be taken from any particular purchaser. However, in the absence of agreement as to these items, it then becomes the primary duty of the common purchaser to devise in good faith a formula, which will be undiscriminatory as to price and ratable take among the various producers in the field. . . (Citations omitted). Once the common purchaser has in the absence of agreement set a price, the question of the good faith of the purchaser and the reasonableness of the basis chosen by it in setting the price may present a question for the Railroad Commission. Primarily, what the order of the Commission does in this case is to determine that Rio Grande is a common purchaser and that as such it must take gas from the Maguire Well in accordance with statutory provisions proscribing discrimination. *The order adopted by the Commission is in proper form to meet the situation as it has so far developed.* It remains to be seen whether further or additional orders will be required. (Emphasis added). (*Id.* at 312).

The applicable provisions of the Texas Common Purchaser Act, which are set forth in *Rio Grande, supra*, provide that a common purchaser of gas "shall purchase [gas] offered to it for purchase without discrimination in favor of one producer or person as against another in the same field." (*Id.* at 308). The provisions of Statewide Rule 48 as promulgated by the Mississippi Oil and Gas Board are very similar.

The United States Supreme Court has also decided that a state ratable take order, although couched in general language, presents no constitutional infirmities regarding vagueness. The Court considered the vagueness issue in *Phillips Petroleum Company v. Oklahoma*, 340 U.S. 190, 95 L.Ed. 204, 71 S.Ct. 221 (1950), a companion case to *Cities Service Gas Company v. Peerless Gas & Oil Company*, 340 U.S. 179, 95 L.Ed. 190, 71 S. Ct. 215 (1950), which, as discussed *supra*, upheld the constitutionality of ratable take statutes and orders. The contention of Phillips was that the ratable take orders issued by the Oklahoma Corporation Commission were unconstitutionally vague. To this assertion the Supreme Court replied:

> In substance, this argument is nothing more than that the determination by an integrated company of proceeds realized from gas at the wellhead involves complicated problems in cost accounting. These problems are common to a host of valid regulations. There is nothing to indicate that Phillips will be penalized for reasonable and good faith efforts to solve them. (340 U.S. at 192).

With respect to the instant case, there is nothing confusing or mysterious about the operation of Statewide Rule 48 or, more specifically, Order No. 409-82. The language of the rule is sufficiently definite to put a purchaser on notice that it shall "purchase without discrimination" within a common source of supply or pool. In the proceedings before the Board, Transco did not contend that it did not understand what Rule 48 meant or required.

Additionally, it is no secret that Transco was aware of the existence of Rule 48 when it first sought to purchase gas from the Greens Creek and East Morgantown Fields. During the Oil and Gas Board hearing, the following discussion took place between Chairman Fancher and Tricia Pollard, Senior Gas Contract Representative for Transco:

> By Chairman Fancher: Okay. Let me ask you a question. When Transco enters into a Gas Purchase Contract, are they aware of the Rule 48?

ANSWER: Yes, sir, when we contract to buy gas in any state, we buy it subject to the rules in the state. Just like when we sent out the letter requesting that the operators cut back to only the gas which was under contract to us.

By Chairman Fancher: Yes, that's all very good, but what about ratable taking without discrimination? When you come in here to purchase gas don't you realize that your contract is subject, and that your purchasing and your distribution and sale of gas, is subject to Rule 48? If the rule is any good it's part of your contract, isn't it? Or at least your operations are subject to it, are they not?

ANSWER: That's correct.

(*Transcript*, at 252-53).

Nor is Order No. 409-82 vague. It contains extensive and specific findings of fact and, as to the discrimination issue, finds that on and after July 1, 1982 Transco has discriminated against Coastal by first refusing to buy Coastal's gas at all, and then offering to buy Coastal's gas on different terms and conditions and at a different and much lower price than that at which Transco proposed to continue buying Getty's and Tomlinson's share of gas from the same pool. The evidence established that the difference in the price ($5.00 per MMBTU) and the terms offered to Coastal, when measured by the price ($7.90 per MMBTU) and the terms extended to Getty and Tomlinson, was discriminatory against Coastal and in favor of Getty and Tomlinson. After taking note of this discrimination, Order No. 409-82 orders Transco to purchase without discrimination. This leaves no reasonable man with any doubt but that Transco, if and when it chooses to buy gas from the pool, shall buy Coastal's gas on the same terms and conditions as it buys Getty's and Tomlinson's gas.

3. The Claim of Taking of Private Property for Private Use Without Compensation

Order No. 409-82 does not constitute a taking of private property for private use without compensation. This notion

was disposed of in *Cities Service Gas Co. v. Peerless Oil & Gas Co., supra.* In that case Cities Service asserted:

> The application thus given to the statute under the relevant facts in the record deprives appellant of its property for the private use and benefit of the royalty owners and certain producers, and is taking of property without due process of law, forbidden by the Fourteenth Amendment. (95 L.Ed., at 194).

The Supreme Court rejected this argument, stating:

> The Due Process and Equal Protection issues raised by appellant are virtually without substance. It is now undeniable that a state may adopt reasonable regulations to prevent economic and physical waste of natural gas. This Court has upheld numerous kinds of state regulation designed to curb waste of natural resources and to protect the correlative rights of owners through ratable taking, *Champlin Refining Co. v. Corporation Commission*, 286 U.S. 210, 76 L.Ed. 1062, 52 S.Ct. 559, 86 ALR 403 (1932), or to protect the economy of the state. *Railroad Commission v. Rowan & Nichols Oil Co.*, 310 U.S. 573, 84 L.Ed. 1368, 60 S.Ct. 1021 (1940). These ends have been held to justify control over production even though the uses to which property may profitably be put are restricted. *Walls v. Midland Carbon Co.*, 254 U.S. 65, L.Ed. 276, 41 S.Ct. 118 (1920).
>
> Like any other regulation, a price fixing order is lawful if substantially related to a legitimate and sought to be attained. *Nebbia v. New York*, 291 U.S. 502, 78 L.Ed. 940, 54 S.Ct. 505, 89 ALR 1469 (1934) and cases therein cited. (340 U.S., at 184-85).

Order No. 409-82 takes no property from Transco. It merely requires that, if and when Transco elects to take gas from the pool in question, Transco must take the quantities it needs ratably from the wells and producers in those wells who want to sell their gas, and purchase that gas without discrimination.

While Transco is free to reach agreements with producers on the terms and price to be paid for the gas, Rule 48 ensures that a producer who wants to sell his gas is not required to sell it at a discriminatory price.

II. STATE LAW CHALLENGES

Transco has asserted that since Statewide Rule 48 is directed toward purchasers of oil and gas, the Oil and Gas Board, which Transco asserts is empowered to regulate only the production of oil and gas, cannot, in the absence of a ratable take statute, promulgate a ratable take rule. To the contrary though, the Court finds that Statewide Rule 48 was promulgated pursuant to the Board's express statutory authority to prevent waste and protect the co-equal and correlative rights of the owners in a common pool, and the state's inherent police powers (delegated to the Board) to protect its producers from discriminatory purchasing practices and to condition the right to conduct business in this state.

Mississippi Code Annotated Section 53-1-1 (1972) declares that it is the policy of the State of Mississippi to:

> . . . protect the public and private interests against the evils of waste in the production and utilization of oil and gas, by prohibiting waste as herein defined; to safeguard, project and enforce the coequal and correlative rights of owners in a common source or pool of oil and gas to the end that each such owner in a common pool or source of supply of oil and gas may obtain his just and equitable share of production therefrom[.] (Emphasis added).

Section 53-1-3(k) (3), Mississippi Code Annotated (Supp. 1982) defines "waste" as:

> Abuse of the correlative rights and opportunities of each owner of oil or gas in a pool due to non-uniform, disproportionate, or unratable withdrawals causing undue drainage between tracts of land or resulting in one or more owners in such pool producing more than his just equitable share of the production from such pool.

Section 53-1-17 empowers the Board to adopt "reasonable rules, regulations and orders" as may be necessary to implement the stated purposes and legislative intentions of the conservation laws of this state. The purposes of those rules expressly include the prevention of "waste" as defined by Section 53-1-3, and the prevention of "reasonably avoidable drainage from each developed unit which is not equalized by counterdrainage."

Statewide Rule 48 provides as follows in its entirety:

> Each person now or hereafter engaged in the business of purchasing oil or gas from owners, operators, or producers shall purchase without discrimination in favor of one owner, operator, or producer against another in the same common source of supply.

At the oral argument of this case, counsel for the parties agreed that Statewide Rule 48 has been on the books of the Board for over thirty (30) years, having been promulgated shortly after passage of the 1948 Conservation Act. This type of rule is sometimes referred to as a "common purchaser rule" and is in force and effect in one form or another in most of the oil and gas producing states in this country, including Oklahoma, Kansas, New Mexico, Florida, North Carolina, Colorado and Louisiana. All of these statutes and rules are designed to protect the co-equal and correlative rights of the owners in a common pool so that each owner has the opportunity to receive his proportionate share of production, and to protect producers from discriminatory purchasing practices and the unequal bargaining position which generally exists between a purchaser and the owners of small undivided interests in a pool. As set forth in *Summers on Oil and Gas*, Volume 1A, Section 103.1 at 132:

> The mere opportunity of a land owner to take his share of the oil and gas in common source of supply does not provide complete protection of his property rights in them. If others produce and market, he must also produce and market or loose much of his share through drainage

> and the exhaustion of reservoir energy. He cannot produce and market unless a market outlet is available. To provide market outlets for both oil and gas a few states have enacted common purchasers statutes requiring common carrier pipelines or other persons in the business of purchasing oil and gas in a common source of supply to take ratably from all owners.

The Mississippi Supreme Court has repeatedly upheld the rule-making powers of the Oil and Gas Board, particularly where a rule of the Board was for the purpose of preventing waste and protecting the co-equal and correlative rights of the owners in a common pool of oil and gas. In *Superior Oil Company v. Foote*, 59 So.2d 85 (Miss. 1952), the Mississippi Supreme Court, in upholding the validity of the compulsory pooling statute, made the following observations:

> . . .The police power of the State includes not only regulations to promote public health, good morals, and good order, but also the right to regulate and promote development of industry and utilization of natural resources in order to add to the wealth and prosperity of the State. (Citations omitted). Hence the courts have consistently held that the State may enact regulatory laws for and prescribe methods of extracting oil and gas for the purposes of conservation, the efficient use of reservoir energy, and the protection of the correlative rights of all owners in a common source of supply. But the statute must not be arbitrary or unreasonable, and the regulation must have a direct, substantial, and reasonable relation to the statutory purpose. *Miss. Const. of 1980*, Sect. 16, provides that "laws impairing the obligation of contracts, shall not be passed." The U.S. Const., Art. I, Sec. 10, cl. 1, has a somewhat similar provision. However, it is well established that this provision is qualified by a proper exercise of the police power of the state. . . Hence it is said that all contracts and property rights are subject to a reasonable exercise of the police power. (*Id.* at 93).

In *California Co. v. State Oil and Gas Board*, 27 So.2d 542 (Miss. 1946), the Board promulgated oil well spacing rules for the Cranfield Field in Adams County, and granted exceptions to those rules. The Mississippi Supreme Court ruled that the well spacing rules and the Board's power to grant exceptions to those rules were valid. Also of interest is *Barnwell, Inc. v. Sun Oil Co.*, 162 So.2d 635 (Miss. 1964) the Board's adoption of "special field rules" for a gas field was challenged on the grounds that there was no expressed statutory authority. However, the court upheld the Board's order as a valid exercise of the Board's police power, commenting that:

> The police power of the state includes not only regulations to promote public health, good morals and good order, but also the right to regulate and promote the development of industry and utilization of natural resources in order to add to the wealth and prosperity of the state. . . The police power of a sovereign state does not find its source in the written constitution of the state, it is a power inherent in the existence of a sovereign government. (162 So.2d at 641).

Transco contends that because the Mississippi conservation laws are directed exclusively toward producers, Rule 48 does not have the "direct, substantial, and reasonable relation to the statutory purpose" necessary to pass judicial scrutiny. Transco has stated that the Board should instead allocate production from the Greens Creek and East Morgantown Fields according to market demand. Transco cites Section 53-3-9(a), Mississippi Code Annotated (1972) for this proposition. This section states:

> Whenever the state oil and gas board has fixed for the purpose of preventing waste, as defined in section 53-1-3, the total amount of oil or gas which may be produced in any pool in this state at an amount less than that amount which the pool can produce, the board shall allocate or apportion the allowable production among the producers in the pool on a reasonable basis so as to prevent reasonably avoidable drainage from each developed unit which is

> not equalized by counter-drainage, and so that each producer will have the opportunity to produce or receive his just and equitable share, as above set forth.

While it is true that the Oil and Gas Board can determine allowables from a common source of supply, the Board has no authority to proration such production according to market demand, as Transco suggests. Indeed, the Board is expressly prohibited from doing so. Section 53-1-1, Mississippi Code Annotated (1972), states:

> *It is not the intent nor the purpose of this law to require or permit the proration or distribution of the production of oil and gas among the fields and pools of Mississippi, on the basis of market demand.* It is the intent and purpose of this law to permit each and every oil and gas pool in Mississippi to be produced up to its maximum efficient rate of production, subject to the prohibition of waste as herein defined and subject further to the enforcement and protection of the co-equal and correlative rights of the owners of a common source of oil and gas, so that each common owner may obtain his just and equitable share of production therefrom. (Emphasis added).

The mandate of the Oil and Gas Board is to prevent waste. If a purchaser's discriminatory purchasing practices cause waste by creating a situation where gas migrates *from* a gas unit from which the purchaser is purchasing less than that unit's allowable production *to* a gas unit from which the purchaser is purchasing that well's entire allowable production, the Board has the duty to intervene and protect those producers whose unit is being drained by unratable taking.

Transco has asserted that the Board's power to prevent waste is limited to the enumerated measures given to it by statute. It cites *Dobson v. Arkansas Oil & Gas Commission*, 235 S.W.2d 33 (1950), for the proposition that "where express powers are granted, the Board cannot adopt substituted measures no matter how desirable." This statement ignores the

plain language of Section 53-1-17(c), Mississippi Code Annotated (Supp. 1982), which states:

> The board shall have the authority, and it shall be its duty, to make, after notice and hearing as hereinafter provided, such reasonable rules, regulations and orders as may be necessary from time to time in the proper administration and enforcement of the provisions of sections 53-1-1 through 53-1-47, inclusive, and sections 53-3-1 through 53-3-21, inclusive, and to amend the same after due notice and hearing, *including but not limited to*, rules and regulations and orders for the following purposes. . . . (Emphasis added).

This statutory language makes it plain that the legislative intent was to clothe the Board with such implied powers as are necessary to prevent waste and to protect the co-equal and correlative rights of producers.

Clearly, the Board's general statutory powers to prevent waste and enforce the co-equal and correlative rights of the owners in a common pool; the Board's express statutory powers to prevent the abuse of the co-equal and correlative rights of the owners in the pool due to unratable withdrawals from a common pool; and the Board's inherent police power, derived from the delegation of that power by the Legislature to the Board, to protect producers from discriminatory purchasing practices and condition the right of purchasers to take oil and gas from this state, empowered the Board to originally adopt Statewide Rule 48 over thirty years ago. As the Mississippi Supreme Court stated in *Mississippi Public Service Commission v. Chambers*, 108 So.2d 550, 554 (Miss. 1959);

> It is the general rule that when a public board such as the Mississippi Public Service Commission is granted certain enumerated powers, there is usually conferred the implied power that may be reasonably necessary to the performance and exercise of the powers expressly granted. 108 So.2d at 554.

It is important to recognize that Rule 48, like the common purchaser rules in other states, lawfully conditions the right of a purchaser to conduct its business of taking and purchasing gas from a common pool in this state. While a purchaser is free to take no gas from a pool or only such quantities of gas as it desires, and is free (at least, initially) to determine the price which it will pay, if the purchaser elects to take gas from the pool, then the purchaser must take and purchase without discriminating among the producers in the pool. Of course, a purchaser and a producer can freely agree to any terms of sale and a producer can agree to sell on "discriminatory" terms; however, under Rule 48 a producer can not be forced to accept a discriminatory price in lieu of not having his gas purchased at all.

It is firmly established that a state has the inherent right to condition the right to conduct a business. For example, in *Nebbia v. People of State of New York*, 291 U.S. 502 (1934), the Supreme Court upheld the constitutionality of state milk control acts which regulated the milk industry and, among other things, fixed the minimum prices for milk:

> The constitution does not guarantee the unrestricted privilege to engage in a business or to conduct it as one pleases. Certain kinds of business may be prohibited; and the right to conduct a business, or to pursue a calling, may be conditioned. Regulation of a business to prevent waste of the state's resources may be justified. * * * So far as the requirement of due process is concerned, and in the absence of other constitutional restrictions, a state is free to adopt whatever economic policy may reasonably be deemed to promote public welfare, and to enforce that policy by legislation adapted to its purpose.* * * The constitution does not secure anyone the liberty to conduct his business in such a fashion as to inflict injury upon the public at large, or upon any substantial group of people. 291 U.S. at 528-29, 537-39.

Nebbia, and the power of a state to condition the right to conduct a business, was recently reaffirmed in *New Motor Vehicle Board of California v. Orrin W. Fox Co.*, 439 U.S. 96 (1978).

The Mississippi Supreme Court has likewise affirmed the principal that a state has the inherent police power to condition the conduct of a business in this state. Thus, in *Mississippi Milk Commission v. Vance*, 129 So.2d 642 (Miss. 1961), the Mississippi Supreme Court upheld the constitutionality of the Mississippi Milk Control Act which, among other things, authorized the Mississippi Milk Commission, a regulatory board to that industry what the Oil and Gas Board is to the oil and gas industry, to regulate and fix the minimum prices of milk sold in this state. The Act was upheld on the grounds that it was a reasonable exercise of the police power of the state and "the police power takes precedence over all private rights even though they stem from constitutional basis." *Id.* at 660.

Thus, it is clear that Transco has never had an unqualified constitutional right to buy gas from a pool in this state. Transco's right to buy gas from a pool in this state is subject to conditions imposed by this state pursuant to either express statutory authority or the inherent police power of the state. The condition which has been imposed upon the "right" of a gas purchaser in this state to purchase from a pool of oil or gas is that the purchaser "purchase without discrimination in favor of one owner, operator or producer against another in the same source of supply."

While not necessarily controlling of the question of the Board's state authority for adopting Statewide Rule 48, the Court believes that it is highly relevant to consider what can only be deemed to be legislative acquiescence in and ratification of Statewide Rule 48. As counsel for all parties have conceded, Statewide Rule 48 has been a rule of the Board for over thirty (30) years. Yet, during that time, the Legislature has not indicated its disapproval of the rule. During the 1982 legislative session, the State Oil and Gas Board underwent

"sunset review" pursuant to Mississippi Code Annotated Section 5-9-9(4), as required by the Mississippi Agency Review Law of 1978, Mississippi Code Annotated Sections 5-9-1 et seq (Supp. 1982), thereby necessarily entailing a legislative review of, *inter alia*, "all powers, duties and functions currently performed by" the Board, and "all constitutional, statutory, or other authority under which said powers, duties and functions" of the Board are carried out. Mississippi Code Annotated Section 5-9-19(b) (c). After this review, the Legislature voted to continue the Board in effect. *See* Chapter No. 485 House Bill No. 473, approved April 23, 1982. In doing so, the Legislature did not indicate its disapproval of Statewide Rule 48.

During the most recent 1983 legislative session, and in what may have been a response to the present challenge to the Board's authority to adopt Statewide Rule 48, the Legislature amended Mississippi Code Annotated Section 53-1-17 to include the following provision:

> (f) The board shall continue to have the power to make rules, regulations and orders necessary to prevent and protect against discrimination and the purchase, production and sale of oil and gas and against the unratable withdrawal of same, *including as provided for in Statewide Rule 48*. (Emphasis added).

This most recent legislative enactment, coupled with the longstanding nature of this rule, is persuasive evidence of the legislative acquiescence in and affirmative ratification of Statewide Rule 48 as a reasonable exercise of the Board's express and implied statutory powers and inherent police powers originally delegated to it by the Legislature in the course of enacting the Conservation Act of 1948. The viable concept of legislative acquiescene in and ratification of a longstanding rule of an administrative agency as being within the agency's powers was most recently reaffirmed by the United States Supreme Court in *Bob Jones University v. United States*, No. 81-3 (U.S. S.Ct. May 24, 1983), and that concept is equally applicable here as supporting the conclusion that the Board was vested with

ample authority as a matter of state law to adopt Statewide Rule 48 and issue Order No. 409-82.

III. THE CLAIMED PROCEDURAL AND EVIDENTIARY ERRORS

In its Assignments of Error 1 through 3, Transco contends that the Board erred in a variety of evidentiary rulings; that the Board was arbitrary and capricious in finding that Transco was discriminating against Coastal et al. in violation of Statewide Rule 48; and that the Board's Order No. 409-82 is not supported by substantial evidence.

In considering these assigned errors, the Court is mindful of the applicable standard of judicial review of an order of the State Oil and Gas Board:

> Whether the order is supported by substantial evidence, is arbitrary or capricious, beyond the power of the Board to make, or violates some constitutional right of complaining party.

California Co. v. State Oil & Gas Board, 200 Miss. 824, 842, 27 So.2d 542, 546 (1946); *Masonite Corp. v. State Oil & Gas Board*, 240 So.2d 446, 448 (Miss. 1970); *Damson Oil Corp. v. Southeastern Oil Co.*, 370 So.2d 225, 229 (Miss. 1979). The findings of an administrative agency like the Board are prima facie correct and the reviewing court may not substitute its judgment for that of the administrative agency where there is a substantial basis in the evidence for the findings. *Barnwell, Inc. v. Sun Oil. Co.*, 162 So.2d 635 (Miss. 1964).

1. The Claimed Evidentiary Errors

The trial before the Board was conducted in accordance with the Board's "Rules of Order and Procedure for Hearings Before the Board." Rule 13(c) thereof provides as follows:

> The materiality, relevancy and competency of any testimony shall be subject to challenge by any party to the hearing or by any member of the Board. When so interposed, such objections shall be acted upon by the Chair-

man or by the acting Chairman, his ruling thereon being subject to change by a majority vote of Board members then sitting.

The issue before the Board was whether Transco was violating Statewide Rule 48 and the conservation laws which prohibit waste. The two factual questions before the Board were fairly simple: (1) Was Transco taking gas unratably from the wells producing from the Harper Sand Gas Pool so as to cause or threaten to cause "waste"? (2) Was Transco discriminating against Coastal et al. and in favor of Getty and Tomlinson in Transco's purchases and takes of gas from that pool?

The record establishes that Transco never denied that it was in fact taking gas unratably from the wells producing the pool, and it admitted that it had, at first, refused to buy the gas of any producer, such as Coastal, who did not already have a gas purchase contract with Transco, and, subsequently, then offered to buy those purchasers' gas at a price which was substantially lower than the price which Transco would continue to pay Getty and Tomlinson, those producers' operators.

To what were almost exclusively undisputed facts on those two factual questions, Transco's defense was an explanation for why it was violating Statewide Rule 48 and state law by taking gas unratably and offering to pay the non-contract owners a discriminatory price: Transco believed that it might not make enough of a profit—or might in some point in the future lose money—if Transco had to pay the non-contract owners the same price which Transco was paying Getty and Tomlinson, those owners' operators. As interesting as Transco's excuse for violating the law might be, the fact is that the Board sustained various objections complained of on the grounds that the testimony or evidence sought to be aduced was speculative or was not relevant or material to the issues in the suit.

As an evidentiary matter, the rulings Transco complains of were made on the grounds that the question or proof were not relevant or material to the simple factual questions as to whether Transco was then violating Statewide Rule 48 and

committing waste. Some rulings went against Transco and some rulings went against Coastal et al. All the evidentiary rulings complained of called for the exercise of judgment and discretion by the Board, taking into consideration the issues. The Court finds that not one of the evidentiary rulings complained of constituted error, much less reversible error.

2. The Claim That the Board Acted Arbitrarily and Capricious In Fighting That Transco Was Discriminating Against Coastal

3. The Claim of Lack of Substantial Evidence

Transco's assignment of error 2 contends that the Board was arbitrary and capricious in finding that Transco was discriminating against Coastal et al. in violation of Statewide Rule 48. Transco's contention is that the Board could not find that Transco violated Rule 48 unless the Board found that Transco's discriminatory purchasing practices were "unreasonable" or "unjust." Transco's third assigned error is that the Order is not supported by subtantial evidence.

At the outset, the Court notes that the conservation statutes in general, and Statewide Rule 48 in particular, do not invite a person to comply with the law if it is convenient or profitable, and do not excuse a violation of the law because the violator believes he is acting "reasonable" or "just." These laws require that person, including Transco, comply with the law. The Board was not required to find that Transco was "unjustly" or "unreasonably" violating the conservation laws and committing waste before it could order Transco to comply with Statewide Rule 48 and stop the waste. The questions were whether Transco was taking gas unratably so as to cause waste, regardless of whether the waste was "reasonable" or "unreasonable", and whether Transco was in fact discriminating against Coastal et al. in favor of the operators, regardless of whether the discrimination was "reasonable" or "unreasonable".

The evidence that Transco was proposing to take gas unratably from the wells producing from the pool so as to cause or result in "waste," including undue drainage between tracts of land, is unrefuted. On May 19, 1982, Transco informed Getty by letter that:

> Effective June 1, 1982, Transco will only take production attributable to the pro rata working interests of the above named signatory parties under the various Getty wells, and until further notice will no longer take any gas being sold by the operator under the Operating Agreement. [Transcript at 49].

After negotiations with Getty, Transco agreed to delay implementing this decision until July 1, 1982. After July 1, however, Transco reduced its takes in this manner. The testimony of Ray Corcoran, Gas Activities Manager for Getty Oil Company, clearly described what occurred:

Q. (Mr. Watters) (for Getty)

I ask if you, Getty Oil Company, in fact, cut the production from the Getty operated wells in the Greens Creek Field and the East Morgantown Field insofar as they related to the Harper Sand Gas Pool after Transco advised them in May or June of 1982 that they should be cut?

A. Yes, we did cut to approximately 70 percent of the well deliverability and this was significantly lower than the June volume.

BY MR. WATTERS:

That's all the questions we have on rebuttal.

Cross Examination

BY MR. STEWART (for Transco):

Q. Mr. Corcoran, when was this production cut?

A. July 1.

Q. What wells were included in the production cut?

A. In the petition—

Q. No, sir, that's not my question. My question is: what wells were cut?

A. We cut all of the Getty operated wells.

Q. How many wells are operated by Getty in the area?

A. Four, with one well being on dual completion.

Q. This cut back to 70 percent includes—is the entire volume—a cut back of the entire volume—a cut back of the entire volume that Getty sold to Transco, is that correct.

A. Yes.

Q. And it also includes—

A. The entire volume in the Newsom, Greens Creek, East Morgantown.

Q. It includes gas that was being produced from other zones, isn't that correct?

A. No, the 70 percent is strictly the Harper Gas Pool.

Q. It does not include the lower zone in the Buckley Well?

A. That pool, the Hosston zone, was cut by the request of your letter.

Q. It was part of the 70 percent?

A. They were both cut 70 percent.

Q. And the cut backs of each well was not necessarily 70 percent though, was it?

A. Yes.

Q. Each well was cut back 70 percent—to 70 percent of its prior month's production?

A. The prior month's production—the 70 percent is of the well deliverability. From the prior month, it would probably be—I'm strictly estimating—probably would be 20 percent.

BY MR. STEWART:

No further questions.

BY MR. TAYLOR (for Coastal):

Q. Is Coastal's share of that gas part of that gas not being produced by the Getty well?

A. Yes, it is.

(*Transcript*, at 353-55).

Getty's reduction in deliveries in response to Transco's cutbacks could have but one result—unratable withdrawals between units. Because of the unratable withdrawals, the producers in the underproduced units would not receive their fair share of production. The undisputed testimony of Gerald Brautigam, who testified as an expert witness for Getty, established the effect of unratable withdrawals:

(BY MR. WATTERS):

Q. In other words, there is no geological feature which would prevent the Harkins Board of Supervisors 16-11 Well in Section 16, the Tomlinson Williamson Well in Section 21, the Florida Exploration Barnes 29-1 Well in Section 29, the Florida Exploration Carlisle 4-2 Well and other wells in the Harper Sand Gas Pool from draining hydrocarbons under the three Getty wells and the Tomlinson Willoughby 3-5 Well in the event the latter wells do not produce in sufficient volumes to offset drainage?

A. That is correct. If the three Getty wells and the Tomlinson Willoughby well are not produced at all, in time the other wells that are completed in the pool would significantly drain the unit in which these wells

are located. If the production from these four wells is lower than the production in the surrounding wells to an extent that drainage is not offset by counter-drainage, then these wells will not produce their co-equal and correlative share of hydrocarbons from the Harper Sand Gas Pool reservoir.

Q. What do you think is necessary for these wells to produce a share which will enable them to recover sufficient production to protect their co-equal and correlative rights of all parties owning an interest in these wells?

A. Well, in my opinion ratable production based on deliverability is necessary. In other words, if the other wells in the pool are producing at their maximum efficient rate of recovery, then these four wells should also be permitted to produce at their maximum efficient rate of recovery to prevent drainage.

* * *

Q. In your opinion if Transco is not required to take ratably from all wells in the field, would the co-equal and correlative rights of all parties owning an interest in this field be protected?

A In my opinion it will not. Without ratable production there will be undue drainage between the units. As a result the owners of interests in this [sic] units which are subject to this drainage will not be able to receive their fair share of hydrocarbons from the Harper Sand Gas Pool.

BY MR. WATTERS:

That's all the questions we have of this witness.

BY CHAIRMAN FANCHER:

All right, Mr. Stewart?

BY MR. STEWART (for Transco):

No questions.

(*Transcript*, at 152-54).

The evidence is clear and undisputed: Transco's unratable takes of gas from the wells producing from the pool was causing and threatening to cause undue drainage between tracts of land—drainage from the Getty and Tomlinson operated units to the Florida operated units—resulting in "waste" and in some owners in the pool receiving more than their fair share of gas. Thus, Board in this respect are not arbitrary and capricious.

With regard to the second question, of whether Transco was discriminating against Coastal et al. in favor of their operators, Getty and Tomlinson, the evidence is uncontradicted that Transco was in fact discriminating against Coastal and those other producers who had no contract with Transco but who wanted to sell to Transco. The evidence establishes that Transco at first refused to buy Coastal et al's gas at all. After Coastal filed its petition with the Oil and Gas Board, Coastal then received a letter from Transco in which Transco offered to buy Coastal's gas at a price which was substantially lower than the price which it would continue to pay to Coastal et al's operators, Getty and Tomlinson ($5.00 per MMBTU vs. $7.90 per MMBTU). To treat these producers differently, when their gas was being produced from the same pool through the same wells and with no qualitative difference from the gas of Getty and Tomlinson, is to discriminate against them in violation of Statewide Rule 48.

In contending that the Board acted arbitrary and capricious, Transco contends that the Board did not use a "standard of reasonableness" in determining what differences in terms and conditions equal discrimination of the kind that is prohibited by Statewide Rule 48. Rule 48 provides in relevant part that a purchaser shall purchase without discrimination "in favor of one owner, operator or producer against another in the same common source of supply." In determining whether Transco was in fact discriminating in violation of Rule 48, the Board determined the question of discrimination by reference to the

terms, conditions and price on which Transco was buying the operators' gas. This was a reasonable basis on which to determine the discrimination question. The evidence was uncontradicted that Getty and Tomlinson were the operators of the wells in question, and that for a period of over fifteen (15) months Transco had taken and paid for Coastal et al's gas produced from these wells on the same terms and conditions as Transco took and paid for the operators' gas produced from the wells, all of which was in accordance with what had been and was then the industry practice. Thus, the Board clearly had a reasonable basis for using the price which Transco was paying Getty and Tomlinson as the price for determining whether Transco's purchases from Coastal et al. at a much lower price would be discrimination within the prohibition of Statewide Rule 48.

* * *

Transco asserts that the producers failed to put on any substantial proof that Transco's "cut-back" of gas from the three wells was the cause of unratable drainage. However, as pointed out above, Getty's witnesses testified that Transco had forced Getty to reduce its deliveries, and that such a reduction in production would cause drainage from the Getty units to the neighboring Florida units from which Transco was taking all producers' gas.

Transco's own witness admitted that cut-backs from the Getty units would result in drainage to other units in the common pool. Tricia Pollard, of Transco, testified as follows during her cross-examination:

> Q. And factually, Transco is taking, for all practical purposes, the deliverability capacity of the Harkins wells in Greens Creek completed into what the Getty geologist testified as a pool common with the Harper Sand Gas Pool; Transco is taking deliverability capacity from those wells.
>
> A. Deliverability capacity, is that what you said?

Q. Yes. Let me rephrase it, if you are having trouble with that. In the Harkins wells completed into this same pool, according to the Getty geologist, is Transco refusing to take the gas of any non-signatory parties to the contract between Harkins and Transco?

A. No, I don't believe we are.

Q. So, that as to the Harkins wells Transco is not proposing to cut those wells back to only the interest of the signatory parties?

A. That's correct.

Q. Meaning that if Transco cut back the Getty wells to only the interest of the signatory parties, but continues to take all of the gas produced from the Harkins wells, regardless of whether it's the gas of the signatory parties, there will be disproportionate withdrawals of gas between the wells; yes or no?

A. Yes.

(*Transcript*, at 236-37).

Additionally, some sixty-four (64) pages of the transcript are devoted to testimony by petroleum geologists and reservoir engineers in regard to the geology of the Harper Sand Gas Pool in question and whether Transco was taking gas unratably among the wells producing from the pool so as to cause unit-to-unit drainage and waste. The testimony was clear and direct to the point that Transco's purchases and takes of only its contract parties' gas from the six wells in question was then resulting in unratable takes of gas and was causing and would cause unit-to-unit drainage, with the result that some owners in the pool would recover more than their fair and equitable share of gas.

When a court reviews a decision of an administrative body such as the Board, which sits as a trier of fact, the rule stated in *First National Bank of Vicksburg v. Martion*, 238 So.2d 856 (Miss. 1970), must be kept in mind. In that case, the Mississippi Supreme Court reversed a Chancery Court decision which had

overturned an order of the State Banking Board. The Court established this rule which applies to all administrative agencies which sit as triers of fact:

> On appeal from an order based upon a factual finding by a trier of facts, as the Banking Board was in this case, this Court accepts the evidence which supports or reasonably tends to support the conclusion upon which the order is based, together with all inferences favorable to it which reasonably may be drawn from the evidence. (*Id.* at 858).

The rule established in the *Martin* case commands a reviewing court to find that the Board's decision was indeed based upon substantial evidence. The testimony given to the Board established that Transco intended to reduce its takes from the Getty units, and that deliveries from the Getty units were reduced to comply with Transco's demands. The testimony supported the Board's conclusion that unratable taking would cause undue drainage between units.

It should also be noted that Transco bases its argument that the Board's Order was not supported by substantial evidence in part upon figures which were not made a part of the record at the Board's hearing. These numbers were put together by Transco after all testimony was heard and the parties had rested, when Transco attempted to offer these figures into evidence during its closing argument. The Board refused to allow Transco to enter this exhibit into evidence. (*Transcript*, at 357). Section 53-1-39, Mississippi Code Annotated (1972), provides that all appeals from an order of the Oil and Gas Board "shall be taken and perfected, heard and determined, either in term time or in vacation on the record, including a transcript of the pleadings and testimony, both oral and documentary, filed and heard before the Board."

The Board is empowered to prevent not only present waste, but also *imminent* waste. *See* Mississippi Code Annotated Section 53-1-17. Testimony which establishes that the effect of the unratable taking was and would be to cause undue drainage within and between units certainly conforms to the require-

ments of "subtantial evidence" sufficient to support the Board's findings of fact that Transco's unratable takes of gas was causing waste and drainage between units.

For the reasons set forth above, the Court finds that the Board did not act arbitrary and capricious, and that Order No. 409-82 is supported by substantial evidence.

CROSS APPEAL OF COASTAL

Coastal originally filed a cross-appeal in this case. However, at the oral argument of this case, counsel for Coastal stated that they did not wish to pursue the cross-appeal and would dismiss it. Thus, the Court does not need to address the assignments of error raised by the cross-appeal.

ORDER

For the reasons stated above in the foregoing Memorandum Opinion, IT IS THEREFORE ORDERED AND ADJUDGED AS FOLLOWS:

1. That the Motion to Strike Attempted Reservation of Federal Claims is sustained.
2. That State Oil and Gas Board Order No. 409-82 is affirmed in its entirety.
3. That the cross-appeal filed herein by Coastal is dismissed.
4. That all costs herein shall be and the same are hereby assessed against Transco.

SO ORDERED AND ADJUDGED on this 28 day of June, 1983.

REUBEN ANDERSON,
Circuit Judge

ATTEST A TRUE COPY
Wm. E. "BILL" McKINLEY,
CIRCUIT CLERK
JUNE 28, 1983

By Sharon M. Haley D.C.

APPENDIX C

BEFORE THE STATE OIL AND GAS BOARD OF MISSISSIPPI

IN RE: PETITION OF COASTAL EXPLORATION, INC. TO REQUIRE TRANSCONTINENTAL GAS PIPE LINE CORPORATION TO RATABLY TAKE AND PURCHASE WITHOUT DISCRIMINATION GAS PRODUCED FROM THE GETTY OIL COMPANY—ROGERS 28-11 WELL NO. 1, THE GETTY OIL COMPANY—SIPP 20-9 WELL NO. 2, AND THE TOMLINSON INTERESTS, INC.—WILLOUGHBY 3-5 WELL NO. 1 IN THE GREENS CREEK AND EAST MORGANTOWN FIELDS, MARION COUNTY, MISSISSIPPI

Docket No. 287-82-418
287-82-467

Order 409-82

FILED FOR RECORD
October 13, 1982
STATE OIL AND GAS BOARD
A. Richard Henderson, Supervisor

ORDER

This day this cause came on for hearing on the Petition of Coastal Exploration, Inc. ("Coastal") and the Joinder Petition of Wiley Fairchild, Rodney Fairchild, and W.R. Fairchild Construction Company, Ltd. (all of whom are hereinafter referred to as the "Fairchilds"), to require Transcontinental Gas Pipe

Line Corporation ("Transco") to comply with Statewide Rule 48 of the Rules and Regulations of this Board with regard to Transco's purchase of gas from a common source of supply in the Greens Creek and East Morgantown Fields of Marion County, Mississippi. The Board having considered the Petition, the responsive pleadings thereto, the evidence and testimony, and the argument of counsel thereon, finds that the Petition is well taken and should be granted.

The Board makes the following findings of fact:

1.

This Board has jurisdiction over the parties and the subject matter of the Petition. Lawful notice of the hearing of this matter has been given in the time and manner required by law and the proofs of publication are on file with this Board.

2.

The following wells are completed into and are producing from the Harper Sand Gas Pool which is a common source of supply ("common pool") of natural gas located in the Greens Creek and East Morgantown Fields of Marion County, Mississippi:

WELL	LOCATION	DATE OF FIRST GAS SALES FROM COMMON POOL
Getty Oil Company-Rogers 28-11 Well No. 1	§ 28-5N-19W Marion County, Miss. Greens Creek Field	April 1981
Getty Oil Company-Sipp 20-9 Well No. 2	§ 20-5N-19W Marion County, Miss. Greens Creek Field	October 1981

Tomlinson Interests Inc.-Willoughby 3-5 Well No. 1	§ 3-T4N-R19W, Marion County, Miss. East Morgantown Field	April 1982
Getty Oil Company-Buckley 33-6 Well No.1	§33-5N-19W, Marion County, Miss. East Morgantown Field	April 1981
Florida Exploration Company-Carlisle 4-2 Well No. 1	§ 4-T4N-R19W Marion County, Miss. East Morgantown Field	April 1982
Florida Exploration Company-Barnes 29-1 Well No. 1	§ 29-5N-19W Marion County, Miss. Greens Creek Field	July 2, 1982

3.

Coastal owns small undivided working interests in four of the foregoing wells which are completed into and producing from the said common pool, to-wit: In the "Rogers" well, a .0261220 leasehold working interest; in the "Sipp" Well, a .0066552 leasehold working interest; in the "Willoughby" Well, a .00468750 leasehold working interest; and in the "Barnes" Well, a .0015625 leasehold working interest. By virtue of its said ownership, Coastal owns and has the right to its fair and equitable share of gas produced from the common pool by the said wells. Coastal participated in drilling each of the said wells, voluntarily paid its share of drilling and completion costs, and has timely and regularly paid its share of operating costs.

4.

All of the wells which are completed into and produce from the said common pool have been classified by this Board as deep, high-cost wells under Section 107(C)(1) of the Natural Gas Policy Act of 1978 (NGPA).

5.

Transco heretofore entered into gas contracts with Getty Oil Company ("Getty") and Tomlinson Interests, Inc. ("Tomlinson") providing for Transco to purchase gas produced from the common pool by the said Rogers, Sipp, and Willoughby Wells, among other wells. Transco also contracted with Florida Exploration Company, the operator of the Carlisle and Barnes wells, to purchase all of the gas produced from the common pool by the Carlisle and Barnes Wells and tendered to Transco by the operator.

6.

From the date of first production from the common pool by the said wells, including the Rogers, Sipp and Willoughby Wells in which Coastal owns interests, and continuing until on or about July 1, 1982, each of the said wells (with the exception of the Florida-Barnes Well which did not begin production until July 2, 1982) produced at its maximum efficient rate of flow and Transco took ratably and purchased without discrimination among the owners in the wells all of the gas produced from the common pool by all of the wells, including Coastal's share of gas. Getty and Tomlinson, as the operators of the Rogers, Sipp, and Willoughby Wells, produced and delivered Coastal's share of gas to Transco and Transco took and purchased Coastal's share of gas on the same terms and conditions at the same price as Transco purchased the said operators' share of gas produced from the common pool by the said wells even though Coastal was not a signatory party to a written gas contract with Transco covering these wells. The operators sold Coastal's share of gas pursuant to the operators' authority under operating agreements and Transco took and purchased Coastal's share of gas on the same terms and conditions and at the same price provided for in the operators' contracts with Transco.

7.

In May 1982, Transco advised Getty that effective with production beginning on and after June 1, 1982 Transco would

no longer take or purchase that gas produced from the common pool by the Rogers and Sipp Wells which was attributable to the interest of Coastal and any other owners in the wells who were not signatory parties (those persons being referred to herein as "non-signatory owners") to gas contracts with Transco, but Transco would continue to take and purchase that gas produced from the common pool by the said wells which was attributable to the interest of the operators and other owners in the wells who were signatory parties to written gas contracts with Transco. At the request of Getty, this date was extended to July 1, 1982. Transco gave Tomlinson a like notice as to the Willoughby Well, to be effective August 19, 1982.

8.

Because of Transco's announced intention to refuse to continue to take and purchase Coastal's and the other non-signatory owners' share of gas produced from the common pool by the said wells, Getty notified Coastal and the other non-signatory owners that effective July 1, 1982 their gas would not be produced from the Rogers and Sipp Wells unless they obtained their own purchaser and their own gas contract. Tomlinson gave Coastal a similar notice as to the Willoughby Well, to be effective August 19, 1982.

9.

Coastal then requested Transco to continue to purchase Coastal's share of gas produced from the common pool by the said wells on the same terms and conditions as Transco purchased gas from the operators of the wells or to give Coastal a contract like Transco had given the operators; however, Transco refused to do so prior to the filing of the Petition in this docket. After the Petition in this docket was filed, Transco then offered to buy Coastal's gas (and the other non-signatory owners' gas) on terms and conditions different from those on which Transco had purchased Coastal's gas (and the other non-signatory owners' gas) prior to July 1, 1982, and different from those on which Transco was continuing to buy the operators'

gas. Two of the major differences were Transco's proposal to purchase Coastal's gas subject to a so-called "market-out clause" and at a price per MMBTU which was substantially lower than the price to be paid by Transco to the operators for the operators' share of gas produced from the same pool through the same wells. Coastal did not agree to this proposal because Coastal believed that the proposal discriminated against Coastal and violated Statewide Rule 48, and that Coastal could not be forced to accept a discriminatory piece and discriminatory conditions.

10.

Effective July 1, 1982 as to the Getty-Sipp and Rogers Wells, and effective August 19, 1982 as to the Tomlinson-Willoughby Well, Transco ceased to take and purchase gas attributable to Coastal's interest and the interests of any other nonsignatory owner in the wells until and unless an owner accepted Transco's different offer. As a result, Transco's takes of gas and the rates of production from the common pool by these wells were "cut back" to below the maximum efficient rate of flow of the wells so that, for all practical purposes, the wells produced only and Transco purchased only a rate of production equal to the operators' and other signatory parties' interest in the maximum efficient rate of flow from the wells. However, as to the Florida-Carlisle and Barnes Wells, Transco continued to take gas from these wells at, for all practical purposes, the maximum efficient rate of flow of the wells and to purchase the non-signatory owners' gas which was produced from these two wells and tendered to Transco by Florida, the operator, on the same terms and conditions and at the same price which Transco paid for the operators' gas produced from these two wells. Thus, while the Sipp, Rogers and Willoughby Wells were cut-back to below their respective maximum efficient rates of flow because of Transco's refusal to take and purchase gas, the Barnes and Carlisle Wells continued to be produced at their respective maximum efficient rates of flow because of Transco's takes and purchases of gas from those wells. The result has been and, if

allowed to continue, will be non-uniform, disproportionate and unratable withdrawals of gas from the common pool causing undue drainage between tracts of land, that is, drainage and undue drainage *from* the Getty and Tomlinson operated units producing from the common pool *to* the Florida operated units producing from the common pool. The result has also been and, if allowed to continue, will be one or more owners in the common pool producing more than their just and equitable share of the production from the pool.

11.

Transco's course of conduct has been to discriminate against the owners (like Coastal) of relatively small undivided working interests in the Sipp, Rogers and Willoughby Wells and the common pool produced by the wells simply because they are owners of relatively small undivided interests. From the date of first production by the wells until on or about July 1, 1982, Transco ratably took and purchased without discrimination the non-signatory owners' gas which was produced from the common pool and tendered to it by the operators on the same terms and conditions and at the same price at which Transco purchased the operators' gas produced from the wells. However, on and after July 1, 1982 in the case of the Sipp and Rogers Wells, and on and after August 19, 1982 in the case of the Willoughby Well, Transco has not ratably taken and purchased without discrimination from the common pool but in fact has discriminated in its purchases of gas from the common pool in favor of the operators and against Coastal, and the other non-signatory parties owning interests in these wells, by first refusing to purchase their gas at all, and then, after the Petition in this docket was filed, offering to purchase their gas but on different terms and conditions and at a different—and much lower—price than that at which Transco had been purchasing their gas and at which Transco proposed to continue purchasing the operators' share of gas produced from the common pool by these same wells. Transco's course of conduct since July 1, 1982 has simply been *not* to "purchase without discrimination

in favor of one owner, operator, or producer against another in the same common source of supply" as required by Statewide Rule 48 of this Board.

12.

The Board finds that Transco's refusal to ratably take and purchase without discrimination Coastal's share of gas produced from the said common pool from which Transco is purchasing the operators' gas produced from the common pool by very same wells and other wells completed into the common pool (1) is discriminatory in favor of the operators against Coastal and thereby violates Rule 48 of the Statewide Rules and Regulations of this Board; (2) constitutes "waste" as defined by Miss. Code Annot. § 53-1-3 because, among other things, it abuses the correlative rights of Coastal in the common pool, results in non-uniform, disproportionate and unratable withdrawals of gas from the common pool causing undue drainage between tracts of land, and will have the effect and result of some owners in the pool producing more than their just and equitable share of gas from the common pool to the detriment of Coastal; and (3) does not protect the co-equal and correlative rights of Coastal in the said common pool of gas, but violates, damages, and infringes upon Coastal's said rights. The Board further finds that such discrimination and waste should be prohibited.

13.

The Fairchild's Joinder Petition filed in this docket seeks for the Fairchilds the same relief sought by Coastal. The Fairchilds are owners of small undivided interests in the Getty-Rogers Well and, having no written contract with Transco, are in the same posture as Coastal, having received the same notices from Getty relative to Transco's refusal to continue purchasing their gas produced from the Rogers Well and having been offered the same type of different proposal as Transco offered Coastal. Therefore, the Board's findings set forth in paragraph 12 above also apply as to the Fairchilds' interests.

14.

Inexco Oil Company ("Inexco") has also made an entry of appearance in this docket pursuant to the statutes and the rules of this Board which liberally allow persons interested in the subject matter to be heard. Inexco is the owner of interests in the Rogers, Sipp, Willoughby and Carlisle Wells and, having no written contract with Transco, is in the same posture as Coastal, having received notices relative to Transco's refusal to continue purchasing Inexco's gas produced from the Rogers, Sipp and Willoughby Wells and having been offered the same type of proposal as Transco offered Coastal. Therefore, the Board's findings set forth in paragraph 12 above also apply as to Inexco's interests.

IT IS, THEREFORE, ORDERED AND ADJUDGED by the State Oil and Gas Board of Mississippi that Transcontinental Gas Pipe Line Corporation ("Transco") is hereby ordered immediately and forthwith to comply with Statewide Rule 48 of the State Oil and Gas Board of Mississippi in its purchases of gas from the said Harper Sand Gas Pool in Greens Creek and East Morgantown Fields, and that, if Transco chooses and elects to take and purchase gas produced from the said common pool and the wells producing therefrom, Transco shall ratably take from the wells producing from the common pool; and shall ratably take and purchase gas without discrimination in favor of one owner, operator or producer against another in the said common source of pool; and, specifically, in the event it so chooses and elects to take and purchase gas produced from the said common pool, Transco shall ratably take and purchase without discrimination in favor of the operators Getty and Tomlinson against Coastal, the Fairchilds, and Inexco.

Dated, this the 16th day of September, 1982.

STATE OIL & GAS BOARD OF MISSISSIPPI

By:_____
CHAIRMAN

STATE OF MISSISSIPPI
COUNTY OF HINDS

I hereby certify that the foregoing is a true and correct copy of Oil & Gas Board Order #409-82
now appearing on file and of record in the office of the State Oil and Gas Board at Jackson, Mississippi.
This the 13th day of October, 1982

A. Richard Henderson

A. RICHARD HENDERSON
Supervisor
State Oil & Gas Board

APPENDIX D

246

MINUTES, SUPREME COURT OF MISSISSIPPI
September Term, 1984

WEDNESDAY, OCTOBER 3, 1984
COURT SITTING

No. 55,071

TRANSCONTINENTAL GAS PIPE LINE CORP.

v.

THE STATE OIL & GAS BOARD OF MISSISSIPPI AND COASTAL EXPLORATION, *et al*

This cause this day came on to be heard on petition for rehearing filed herein and this Court having sufficiently examined and considered the same and being of the opinion that the same should be denied doth order that said petition be and the same is hereby Denied. Patterson, C. J., Bowling and Hawkins, JJ., not participating.

ATTEST
A True Copy
This the 8th day of Oct., 1984

ROBERT E. WOMACK
Clerk
SUPREME COURT OF MISSISSIPPI

By Yvonne Burnham, D.C.
Minute Book "BX", Page 246.

APPENDIX E

205

MINUTES, SUPREME COURT OF MISSISSIPPI
March Term, 1984

WEDNESDAY, SEPTEMBER 5, 1984
COURT SITTING

No. 55,071

TRANSCONTINENTAL GAS PIPE LINE CORP.
v.
THE STATE OIL & GAS BOARD OF MISSISSIPPI AND
COASTAL EXPLORATION, INC., *et al*

This cause having been submitted at a former day of this Term on the record herein from the Circuit Court of Hinds County and this Court having sufficiently examined and considered the same and being of the opinion that there is error therein doth order and adjudge that the judgment of said Circuit Court rendered in this cause on the 28th day of June, 1983, be and the same is hereby Affirmed in part, Reversed and Rendered in part and Remanded; all as fully set out in the opinion of this Court with directions. It is further ordered that the taxable costs before this court, before the Circuit Court and before the Board shall be; and they hereby are taxed one-half against Transco, as appellant, and one-half against appellees, jointly and severally for all of which let execution issue.

ATTEST
A True Copy
This the 8th day of Oct., 1984
ROBERT E. WOMACK
Clerk
SUPREME COURT OF MISSISSIPPI
By Yvonne Burnham, D.C.
Minute Book "BX", Page 205.

APPENDIX F

IN THE SUPREME COURT OF THE STATE OF MISSISSIPPI

No. 55,071

TRANSCONTINENTAL GAS PIPE LINE CORPORATION
Appellant,

VS.

THE STATE OIL AND GAS BOARD OF MISSISSIPPI AND COASTAL EXPLORATION, INC., *et al.*,
Appellees.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Transcontinental Gas Pipe Line Corporation, appellant in the above styled cause, hereby appeals to the Supreme Court of the United States from the Order and Judgment of this Court, entered September 5, 1984, rehearing denied, October 3, 1984, which found that "Rule 48" and "Order No. 409-82" of the Mississippi State Oil and Gas Board were not repugnant to the Supremacy Clause, Commerce Clause, and Fourteenth Amendment of the Constitution of the United States.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

This 30th day of November, 1984.

TRANSCONTINENTAL GAS
PIPE LINE CORPORATION

By:_____
One of its Attorneys

Of Counsel:
JOHN M. GROWER
JEFFERSON D. STEWART
R. WILSON MONTJOY, II
BRUNINI, GRANTHAM, GROWER & HEWES
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Telephone: (601) 948-3101

DAVID E. VARNER
RAY V. LOFTIN, JR.
DAVID A. GLENN
TRANSCONTINENTAL GAS PIPE LINE CORPORATION
Post Office Box 1396
Houston, Texas 77251
Telephone: (713) 439-2328

CERTIFICATE OF SERVICE

I, JEFFERSON D. STEWART, do hereby certify that I have this day mailed a true and correct copy of the above and foregoing Notice of Appeal to the following:

Hon. Lloyd Arnold
Office of the Attorney General
Gartin Justice Bldg.
Jackson, MS 39201
Attorney for Mississippi State Oil
and Gas Board

Hon. Glenn Gates Taylor
Heidelberg, Woodliff & Franks
Suite 1030 Capitol Towers
Jackson, MS 39201
Attorney for Coastal Exploration Inc.

Hon. Walker L. Waters
Gerald, Brand, Watters, Cox & Hemleben
400 Lamar Life Bldg.
Jackson, MS 39201
Attorney for Getty Oil Company

Hon. John Land McDavid
McDavid, Edmonson & Noblin
8th Floor, City Center North
210 S. Lamar Street
Jackson, MS 39201
Attorney for Inexco Oil Company

Hon. William L. Waller, Sr.
Waller & Waller
475 East Capitol Street
Jackson, MS 39201
Attorney for Fairchild Construction
Company

I further certify that I have also mailed a copy of the above Notice to Hon. Vernon L. Terrell, Jr., Plauche', Hartley, LaPeyre & Ottinger, Suite 3618 One Shell Square, New Orleans, LA 70139, Attorney for Tomlinson Interests, Inc.

THIS 30th day of November, 1984.

_____

Jefferson D. Stewart

APPENDIX G

FEDERAL CONSTITUTIONAL AND STATUTORY PROVISIONS

The Commerce Clause of the Constitution, U.S. Const. art. I, § 8, cl. 3:

> The Congress shall have power . . . to regulate commerce with foreign Nations, and among the several states, and with the Indian Tribes . . . .

The Supremacy Clause of the Constitution, U.S. Const. art VI, cl. 2:

> **SUPREME LAW OF LAND**
>
> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Section 1(b) of the Natural Gas Act, 15 U.S.C. § 717(b):

> (b) The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation for sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

Section 107 of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3317:

CEILING PRICE FOR HIGH-COST NATURAL GAS

(a) **Wells completed below 15,000 feet.**—In the case of any first sale of high-cost natural gas produced from any well the surface drilling of which began on or after February 19, 1977, if such production is from any completion location which is located at a depth of more than 15,000 feet, the maximum lawful price under this section for such natural gas delivered during any month shall be the maximum lawful price, per million Btu's, computed for such month under section 3312 of this title (relating to new natural gas).

(b) **Commission authority to prescribe higher incentive prices.**—The Commission may, by rule or order, prescribe a maximum lawful price, applicable to any first sale of any high-cost natural gas, which exceeds the otherwise applicable maximum lawful price to the extent that such special price is necessary to provide reasonable incentives for the production of such high-cost natural gas.

(c) **Definition of high-cost natural gas.**—For purposes of this section, the term "high-cost natural gas" means natural gas determined in accordance with section 3413 of this title to be—

(1) produced from any well the surface drilling of which began on or after February 19, 1977, if such production is from a completion location which is located at a depth of more than 15,000 feet;

(2) produced from geopressured brine:

(3) occluded natural gas produced from coal seams;

(4) produced from Devonian shale; and

(5) produced under such other conditions as the Commission determines to present extraordinary risks or costs.

(d) **Provisions for high-cost natural gas to be elective.**—If any credit, exemption, deduction, or comparable adjustment applicable to the computation of any Federal tax is specifically allowable with respect to any high-cost natural gas (or category thereof) under any provision of law enacted after November 9, 1978, the provisions of subsections (a) and (b) of this section and the provisions of part B of this subchapter shall not apply to such natural gas produced from any well unless an election to have such provisions apply (in lieu of such credit, exemption, deduction, or adjustment) with respect to such natural gas produced from such well is filed with the Commission on or before the later of—

(A) the 30th day after November 9, 1978, under which such credit, exemption, deduction, or adjustment is provided; or

(B) the date the surface drilling of such well began.

Section 121 of the NGPA, 15 U.S.C. § 3331:

ELIMINATION OF PRICE CONTROLS FOR CERTAIN NATURAL GAS SALES

(a) **General rule.**—Subject to the reimposition of price controls as provided in section 3332 of this title, the provisions of part A of this subchapter respecting the maximum lawful price for the first sale of each of the following categories of natural gas shall, except as provided in subsections (d) and (e) of this section, cease to apply effective January 1, 1985:

(1) **New natural gas.**—New natural gas (as defined in section 3312(c) of this title).

(2) **New, onshore production wells.**—Natural gas produced from any new, onshore production well (as

defined in section 3313(c) of this title), if such natural gas—

(A) was not committed or dedicated to interstate commerce on April 20, 1977; and

(B) is produced from a completion location which is located at a depth of more than 5,000 feet.

(3) **Intrastate contracts in excess of $1.00.**—Natural gas sold under an existing contract, any successor to an existing contract, or any rollover contract, if—

(A) such natural gas was not committed or dedicated to interstate commerce on November 8, 1978; and

(B) the price paid for the last deliveries of such natural gas occurring on December 31, 1984, or, if no deliveries occurred on such date is higher than $1.00 per million Btu's.

(b) **High-cost natural gas.**—Effective beginning on the effective date of the incremental pricing rule required under section 3341 of this title, the provisions of part A of this subchapter respecting the maximum lawful price for the first sale of natural gas shall cease to apply to the first sale of high-cost natural gas which is described in section 3317(c) (1), (2), (3), or (4) of this title.

(c) **Natural gas produced from 5,000 or less.**—Effective beginning July 1, 1987, or, if later, the date of expiration of any price controls reimposed under section 3332 of this title, the provisions of part A of this subchapter respecting the maximum lawful price for any first sale of natural gas shall, except as provided in subsection (d) of this section, cease to apply to any first sale of natural gas produced from any new, onshore production well (as defined in section 3313(c) of this title), if such natural gas—

(1) was not committed or dedicated to interstate commerce on April 20, 1977; and

(2) is produced from a completion location which is located which is located at a depth of 5,000 feet or less.

(d) **Exclusion of certain Alaska natural gas.**—The provisions of subsections (a) and (c) of this section shall not apply to any natural gas produced from the Prudhoe Bay Unit of Alaska and transported through the natural gas transportation system approved under the Alaska Natural Gas Transportation Act of 1976.

(e) **Limitation on indefinite price excalators.**—Natural gas which is not subject to maximum lawful prices under part A of this subchapter solely by reason of subsection (a) (3) of this section and which is sold under any existing contract or successor to an existing contract at a price established under an indefinite price escalator clause (as defined in section 3315(b) (3) (B) of this title) shall be subject to the provisions of section 3315(b) (3) of this title.

Section 601 of the NGPA, 15 U.S.C. § 3431:

COORDINATION WITH NATURAL GAS ACT

(a) **Jurisdiction of Commission under Natural Gas Act.—**

(1) **Sales.—**

(A) **Natural gas not committed or dedicated.—** For purposes of section 1(b) of the Natural Gas Act, effective on the first day of the first month beginning after November 9, 1978, the provisions of the Natural Gas Act and the jurisdiction of the Commission under such Act shall not apply to natural gas which was not committed or dedicated to interstate commerce as of November 8, 1978, solely by reason of any first sale of such natural gas.

(B) **Committed or dedicated natural gas.—** Effective beginning on the first day of the first month

beginning after November 9, 1978, for purposes of section 1(b) of the Natural Gas Act, the provisions of such Act and the jurisdiction of the Commission under such Act shall not apply solely by reason of any first sale of natural gas which is committed or dedicated to interstate commerce as of November 8, 1978, and which is—

(i) high-cost natural gas (as defined in section 3317(c) (1), (2), (3), or (4) of this title);

(ii) new natural gas (as defined in section 3312(c) of this title); or

(iii) natural gas produced from any new, onshore production well (as defined in section 3313(c) of this title).

(C) **Authorized sales or assignments.**—For purposes of section 1 (b) of the Natural Gas Act, the provisions of the Natural Gas Act and the jurisdiction of the Commission under such Act shall not apply by reason of any sale of natural gas—

(i) authorized under section 3362(a) or 3371(b) of this title; or

(ii) pursuant to any assigned authorized under section 3371(a) of this title.

(D) **Natural-gas company.**—For purposes of the Natural Gas Act, the term "natural-gas company" (as defined in section 2(6) of such Act) shall not include any person by reason of, or with respect to, any sale of natural gas if the provisions of the Natural Gas Act and the jurisdiction of the Commission do not apply to such sale solely by reason of subparagraph (A), (B), or (C) of this paragraph.

(E) **Alaskan natural gas.**—Subparagraph (B) (ii) and (iii) shall not apply with respect to natural gas produced from the Prudhoe Bay unit of Alaska and

transported through the transportation system approved under the Alaska Natural Gas Transportation Act of 1976.

(2) **Transportation.—**

(A) **Jurisdiction of the Commission.** For purposes of section 1(b) of the Natural Gas Act the provisions of such Act and the jurisdiction of the Commission under such Act shall not apply to any transportation in interstate commerce of natural gas if such transportation is—

(i) pursuant to any order under section 3362(c) or section 3363(b), (c), (d), or (h) of this title; or

(ii) authorized by the Commission under section 3371(a) of this title.

(B) **Natural-gas company.** For purposes of the Natural Gas Act, the term "natural-gas company" (as defined in section 2(6) of such Act) shall not include any person by reason of, or with respect to, any transportation of natural gas if the provisions of the Natural Gas Act and the jurisdiction of the Commission under the Natural Gas Act do not apply to such transportation by reason of subparagraph (A) of this paragraph.

(b) **Charges deemed just and reasonable.**

(1) **Sales.**

(A) **First sales.** Subject to paragraph (4), for purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any first sale of natural gas shall be deemed to be just and reasonable if—

(i) such amount does not exceed the applicable maximum lawful price established under subchapter I of this chapter; or

(ii) there is no applicable maximum lawful price solely by reason of the elimination of price controls pursuant to part B of subchapter I of this chapter.

(B) **Emergency sales.** For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any sale authorized under section 3361(a) of this title shall be deemed to be just and reasonable if such amount does not exceed the fair and equitable price established under such section and applicable to such sale.

(C) **Sales by intrastate pipelines.** For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any sale authorized by the Commission under section 3371(b) of this title shall be deemed to be just and reasonable if such amount does not exceed the fair and equitable price established by the Commission and applicable to such sale.

(D) **Assignments.** For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid pursuant to the terms of any contract with respect to that portion of which the Commission was authorized an assignment authorized under section 3372(a) of this title shall be deemed to be just and reasonable if such amount does not exceed the applicable maximum lawful price established under subchapter I of this chapter.

(E) **Affiliated entities limitation.** For purposes of paragraph (a), in the case of any first sale between any interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

(2) **Other charges.—**

(A) **Allocation.**—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid by any interstate pipeline for transportation, storage, delivery or other services provided pursuant to any order under section 3363(b), (c), or (d) of this title shall be deemed to be just and reasonable if such amount is prescribed by the President under Section 3363(h)(1) of this title.

(B) **Transportation.**—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid by any interstate pipeline for any transportation authorized by the Commission under section 3371(a) of this title shall be deemed to be just and reasonable if such amount does not exceed that approved by the Commission under such section.

(c) **Guaranteed passthrough.—**

(1) **Certificate may not be denied based upon price.**—The Commission may not deny, or condition the grant of, any certificate under section 7 of the Natural Gas Act based upon the amount paid in any sale of natural gas, if such amount is deemed to be just and reasonable under subsection (b) of this section.

(2) **Recovery of just and reasonable prices paid.**—For purposes of sections 4 and 5 of the Natural Gas Act, the Commission may not deny any interstate pipeline recovery of any amount paid with respect to any purchase of natural gas if—

(A) under subsection (b) of this section, such amount is deemed to be just and reasonable for purposes of sections 4 and 5 of such Act, and

(B) such recovery is not inconsistent with any requirement of any rule under section 3341 of this title

(including any amendment under section 3342 of this title),

except to the extent the Commission determines that the amount paid was excessive due to fraud, abuse, or similar grounds.

Section 602 of the NGPA, 15 U.S.C. § 3432:

EFFECT ON STATE LAWS

(a) **Authority to prescribe lower maximum lawful prices.**—Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this chapter.

(b) **Common carriers.**—No person shall be subject to regulation as a common carrier under any provision of Federal or State law by reason of any transportation—

(1) pursuant to any order under section 3362(c) or section 3363(b), (c), (d), or (i) of this title; or

(2) authorized by the Commission under section 3371(a) of this title.

STATE STATUTES AND REGULATIONS

Miss. Code Ann. § 53-1-1 (1972):

DECLARATION OF POLICY.

It is hereby declared to be in the public interests to foster, encourage and promote the development, production and utilization of the natural resources of oil and gas in the State of Mississippi; and to protect the public and private interests against the evils of waste in the production and utilization of oil and gas, by prohibiting waste as herein defined; to safeguard, protect and enforce the coequal and correlative rights of owners in a common source

or pool of oil and gas to the end that each such owner in a common pool or source of supply of oil and gas may obtain his just and equitable share of production therefrom; and to obtain, as soon as practicable, consistent with the prohibition of waste, the full development by progressive drilling of other wells in all producing pools of oil and gas or of all pools which may hereafter be brought into production of such, within the state, until such pool is fully defined.

It is not the intent nor the purpose of this law to require or permit the proration or distribution of the production of oil and gas among the fields and pools of Mississippi, on the basis of market demand. It is the intent and purpose of this law to permit each and every oil and gas pool in Mississippi to be produced up to its maximum efficient rate of production, subject to the prohibition of waste as herein defined, and subject further to the enforcement and protection of the co-equal and correlative rights of the owners of a common source of oil and gas, so that each common owner may obtain his just and equitable share of production therefrom.

Statewide Rule 48 of the Mississippi State Oil and Gas Board:

RATABLE TAKE

Each person now or hereafter engaged in the business of purchasing oil or gas from owners, operators, of producers shall purchase without discrimination in favor of one owner, operator, or producer against another in the same common source of supply.

APPENDIX H

BEFORE THE CORPORATION COMMISSION OF THE STATE OF OKLAHOMA

IN RE: WHETHER the AUTHORITY to REQUIRE RATABLE TAKE of NATURAL GAS by FIRST PURCHASERS who are INTERSTATE PIPELINES.

Gen. Cause No. 28770

NOTICE OF INQUIRY
AND
MOTION TO CONSOLIDATE CAUSES

STATE OF OKLAHOMA TO: All persons, owners, producers, operators, purchasers and takers of oil and gas, and all other interested persons in the State of Oklahoma.

Several causes pending before the Oklahoma Corporation Commission concern the Commission's right to exercise jurisdiction over purchases by interstate pipelines which purchase natural gas produced in Oklahoma.

COMES NOW M. Keywood Deese, Deputy General Counsel for Conservation for the Oil and Gas Conservation Division of the Oklahoma Corporation Commission, and moves to consolidate all causes currently filed and pending on or before the date this motion is acted upon, which concern the Corporation Commission's jurisdiction with respect to ratable takes, pursuant to the Oklahoma Statutes and the Corporation Commission rules and regulations, by first purchasers which are interstate pipelines.

The pending causes involve the following issues:

(1) Is the State of Oklahoma preempted by the Commerce Clause of the United States Constitution from enforcing the requirements of 52 O.S. § 240, relating to the ratable taking of gas, against first purchases by interstate pipelines of Oklahoma-produced natural gas.

(2) Does the Federal Energy Regulatory Commission under the Natural Gas Act of 1938 and Natural Gas Policy Act of 1978 have sole authority over the regulation of gas purchases by interstate purchasers of natural gas thereby preempting the State of Oklahoma from acting under 52 O.S. 1981, Sections 239 and 240?

(3) Do interstate pipelines, when making first purchases of natural gas produced in Oklahoma, have to comply with Rule 1-305, a *Priority Schedule for Supply and Demand Imbalance*, adopted in Order No. 246797 issued on October 19, 1983?

Inasmuch as many pending causes involving these common issues of law, and in order to assure as wide an opportunity to participate as possible in the Commission's ultimate determination of those common issues, the Oil and Gas Conservation Division recommends that all currently pending causes that have contained in them the above-stated issues be consolidated into one proceeding and that proceeding be phased into two parts. The first phase would be a Commission decision, following briefing and oral argument by all interested parties, on the above-stated issues of law common to all causes. In the second phase, the cases would be separated for any further necessary proceedings on an individual basis.

In more specificity, it is moved:

(1) That all parties who have filed Causes involving the above questions of law continue said Causes to the 1st day of April, 1984.

(2) That additional cases filed involving these questions be also set on the 1st day of April, 1984.

(3) That the Commission consolidate all such causes and establish an initial thirty (30) day briefing period and a fifteen (15) day reply briefing schedule to be followed by oral argument to a panel of three hearing officers to be designated by the Chief Hearing Officer. The panel would issue a report to which exceptions could be taken in oral and written manner before the Commission.

The staff makes this motion in an effort to seek resolution of this singularly important question of law through a procedure that is at once both administratively efficient and open to participation by all potentially affected and otherwise interested parties. The Commission decision reached herein will be dispositive of these questions before the Commission respecting the consolidated causes and serve as precedential value in future causes of this nature.

All parties wishing to be heard on this motion should appear before the Commission on the 22 day of February, 1984, at 9:00 a.m. in Courtroom 301.

For information concerning this Notice and Motion, contact M. Keywood Deese, Deputy General Counsel for Conservation, Room 460, Oklahoma Corporation Commission, Jim Thorpe Building, Oklahoma City, Oklahoma 73105, Telephone (405) 521-2255.

Respectfully submitted,

M. Keywood Deese
Deputy General Counsel
For Conservation

BEFORE THE CORPORATION COMMISSION OF THE STATE OF OKLAHOMA

IN RE: WHETHER THE OKLAHOMA CORPORATION COMMISSION HAS THE AUTHORITY TO REQUIRE RATABLE TAKE OF NATURAL GAS BY FIRST PURCHASERS WHO ARE INTERSTATE PIPELINES.

Gen. Cause No. 28770
Order No. 254451

ORDER CONSOLIDATING CAUSES

On February 22, 1984, a Notice of Inquiry and Motion to Consolidate Causes came on for hearing before the Oklahoma Corporation Commission sitting en banc. The Notice and Motion were filed by M. Keywood Deese, Deputy General Counsel for Conservation; appearing for the Oil and Gas Conservation Division. Other appearing parties are listed in the Secretary's official record in this cause.

FINDINGS AND ORDER

1. The Deputy General Counsel for Conservation moved to consolidate several pending causes which concern the Commission's jurisdiction with respect to ratable takes, pursuant to the Oklahoma Statutes and the Corporation Commission rules and regulations, by first purchasers which are interstate pipelines.

2. The Commission finds that inasmuch as these causes involve common issues of law and in order to assure as wide an opportunity to participate as possible in the Commission's ultimate determination of those common issues, that these causes shall be consolidated into one proceeding which will be divided into two phases. The first phase will involve a Commission

determination as to jurisdiction after a review of a Report from the Hearing Officers and in the second phase, all cases will be separated and continued for any further necessary proceedings on an individual basis before a Trial Examiner.

3. The Commission hereby finds that issue number three included in the Notice of Inquiry is not necessary to a determination of the jurisdiction of the Commission. The Commission further finds that the request of Cities Service Oil and Gas Corp. to add an additional question relating to question number three is therefore unnecessary.

4. The Commission finds that the two issues which shall be reviewed on a consolidated basis from the pending causes are:

(1) Is the State of Oklahoma preempted by the Commerce Clause of the United States Constitution from enforcing the requirements of 52 O.S. 1981, § 240, relating to the ratable taking of gas, against first purchases by interstate pipelines of Oklahoma-produced natural gas?

(2) Does the Federal Energy Regulatory Commission under the Natural Gas Act of 1938 and Natural Gas Policy Act of 1978 have sole authority over the regulation of gas purchases by interstate purchasers of natural gas thereby preempting the State of Oklahoma from acting under 52 O.S. 1981, § § 239 and 240?

5. The procedures to be followed during phase one of these proceedings are as follows:

(1) All currently pending causes and any additional causes filed involving the above enumerated issues shall be continued or set for hearing on or after July 2, 1984.

(2) By March 16, 1984, any interested party in these proceedings shall file an *original* and *one copy of a Notice of Appearance* in the Secretary's office, including a current mailing address for all pleadings and notices. The Commission requests, but does not hereby order, that all parties filing the Notice of Appearance

include thereon an election as to alignment on the issue of the Commission's jurisdiction in these cases.

(3) That all interested parties may file a brief in this cause dealing with the above issues by March 30, 1984.

(4) That reply briefs shall be filed by May 1, 1984.

(5) All briefs filed according to (3) and (4) above shall be mailed by the filing party to all other parties who have filed a Notice of Appearance. The Secretary of the Commission shall maintain the official mailing list.

(6) That the Chief Hearing Officer shall appoint three Hearing Officers to hear oral argument of the parties on May 21, 1984, at 10:00 a.m. in Courtroom 301. These Hearing Officers shall review the briefs and arguments and issue a Report which if appealed, said appeal shall be heard by the Commission en banc.

6. It is ordered that this Order be published and notice sent as required by law and the Rules of the Commission.

7. The Commission further orders that any final order issued by the Commission in these proceedings shall be a determination of the jurisdictional issues presented in the individual cases consolidated and of precedential value in future causes filed regarding these issues.

DONE AND PERFORMED the 27 day of February, 1984.

CORPORATION COMMISSION OF OKLAHOMA

_____

Hamp Baker Chairman

_____

Norma Eagleton, Vice-Chairman

_____

James B. Townsend, Commissioner

ATTEST:

_____

Berdee S. Holt, Secretary

APPENDIX I

TITLE 16. ECONOMIC REGULATION

Part I. Railroad Commission of Texas
Chapter 3. Oil and Gas Division
Conservation Rules and Regulations

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16 TAC §§ 3.28, 3.30, 3.31

(Editor's note: The text of the following rules proposed for repeal will not be published. The rules may be examined in the offices of the Railroad Commission of Texas, 1124 IH 35 South, Austin, or in the Texas Register office, Room 503E, Sam Houston Building, 201 East 14 Street, Austin.)

The Railroad Commission of Texas proposes the repeal of §§ 3.28, 3.30, and 3.31, concerning gas well potentials, gas nominations, and gas well allowables. The repeal will allow adoption of new versions of the rules.

Patrick Thompson, Oil and Gas Division legal examiner, has determined that for the first five-year period the repeal will be in effect there will be no fiscal implications for state or local government or small businesses as a result of the repeal.

Mr. Thompson also has determined that for each year of the first five years the repeal as proposed is in effect the public benefit anticipated as a result of the repeal is accommodation for the adoption of new sections. The merits of the new sections are discussed.

The Railroad Commission of Texas proposes new §§ 3.28, 3.30, and 3.31, concerning gas well potentials, gas nominations, and gas well allowables, respectively. The proposed new sections are designed to provide for more fair and accurate regulation of gas production and allocation.

Patrick Thompson, Oil and Gas Division legal examiner, has determined that for the first five-year period the rules will be in effect there will be no fiscal implications for state or local government or small businesses as a result of enforcing or administering the rules.

Mr. Thompson also has determined that for each year of the first five years the rules as proposed are in effect the public benefit anticipated as a result of enforcing the rules as proposed is increased understanding of the new sections, more fair and accurate gas proration through more accurate and reliable deliverability tests and more fair nominations, and improved conservation through changes in priority for gas production. The anticipated economic cost to individuals who are required to comply with the rules as proposed will not vary from those under the rules simultaneously proposed for repeal.

Comments on the proposed new sections may be submitted to Patrick Thompson, Legal Section, Oil and Gas Division, Railroad Commission of Texas, P.O. Drawer 12967, Austin, Texas 78711.

[9 TexReg 4808, September 11, 1984]

The new sections are proposed under the Texas Natural Resources Code, §§ 86.041, 86.042, and 86.081, which provides the Railroad Commission of Texas with the authority to prorate and regulate the production of natural gas to prevent waste and adjust the correlative rights and opportunities of owners of gas to use or sell their gas.

§ 3.28 *Deliverability of Gas Wells to Be Ascertained and Reported.*

(a) The absolute daily open flow potential of each producing associated or nonassociated gas well shall be ascertained and a report shall be filed in duplicate in the appropriate district office within 30 days of the completion of the well. The absolute daily open flow potential shall be determined in accordance with the instructions contained in the commission's publication, *Back Pressure Test for Natural Gas Wells, State of Texas,*

and shall be reported on the commission's prescribed form. Any backdating of allowables will be performed in accordance with § 3.31 of this title (relating to Gas Well Allowables).

(b) After conducting the test required by subsection (a) of this section, each operator of a gas well shall conduct an initial deliverability test not later than 10 days after the state of production for one or more legal purposes and shall report such initial deliverability on the prescribed form. After the original deliverability tests have been conducted, each operator of a gas well shall conduct a deliverability test semiannually, unless otherwise provided by the applicable field rules. All deliverability tests shall be conducted in accordance with subsection (c) of this section and the instructions printed on the Form G-10. The results of each test shall be attested to by the operator or his appointed agent and by a designated representative of the purchaser, in the place provided on the Form G-10. Gas meter charts, printouts, or other documents showing the actual measurement of the gas produced during any deliverability test conducted under this section shall be preserved by the maker for a period of no less than two years after the performance of the test and shall be furnished to the Railroad Commission of Texas, operator, or purchaser upon request. In the event that the purchaser refuses to sign the G-10 form and both parties cannot agree upon the validity of the test results, then either party may request a retest of the well. The retest will be witnessed by a representative of the commission and will be scheduled within seven working days of the request, if possible. The results of a commission-witnessed test shall be conclusive for the purposes of this section until the next regularly scheduled test of the well. In the event a retest is performed by the commission, the retest shall be signed by the representative of the commission. In the event that downhole remedial work or a compressor, pumping unit, or other substantial production enhancement work has been performed on any well subject to the testing procedure described in this subsection, then a new test may be requested and shall be

performed according to the procedure outlined in this subsection.

(c) Unless the director of the Oil and Gas Division or his delegate grants an exception due to limited production capacity, all deliverability tests shall be performed by producing the subject well for a minimum time period of 72 hours. The average daily producing rate for each 24-hour period, the wellhead pressure before the commencement of the 72-hour test, and flowing wellhead pressure at the beginning of each 24-hour period shall be recorded and reported as required on the Form G-10. In addition, a 24-hour shut in the wellhead pressure shall be recorded on the Form G-10 either before or after the flow test. The flow rate during the first 48 hours of the test must be as close as possible to the flow rate during the final 24 hours of the test, but must equal at least 75% of such flow rate. The deliverability of the well during the last 24 hours of the flow test shall be used for allowable and allocation purposes. Deliverability tests shall be scheduled by either the producer or purchaser with the concurrence of the other and within the testing period designated by the Railroad Commission of Texas. A deliverability test shall be conducted under normal and usual operating conditions using the normal and usual operating equipment in place on the well being tested, and produced against the normal and usual line pressure prevailing in the line into which the well produces.

(d) First purchasers with packages of gas dedicated entirely to a downstream purchaser shall coordinate testing with and provide test results to that downstream purchaser if requested by the downstream purchaser. In such cases, the downstream purchaser shall have the right to witness all deliverability tests and retests.

(e) The appropriate district office shall be notified at least 24 hours prior to any back pressure, production, or shut-in test. Tests of wells connected to a pipeline shall be made in such manner that no gas is flared.

§ 3.30. *Gas Nominations Required.*

(a) All first purchasers of gas produced from wells shall file by the ninth day of each month nominations of requirements for gas to be used by them from each reservoir during the following month. Purchasers who gather gas from various gas fields and reservoirs or who purchase gas at the wellhead of the wells or purchase gas at a common purchase point must determine if they are the initial purchaser and, if so, shall file gas nominations. An operator using 100% of the gas from a gas well for his own operations, either on leases or in a fuel system, shall file gas nominations. An operator using a portion of the gas produced from a well must notify the nominator of the volume or percentage of total volume required, including lease separation extraction or percentage loss. The initial nominator must include that amount in its nominations. After initial notification, the operator need only inform the nominator of changes in the volume or percentage of total volume required. Operators of processing plants who operate field gathering systems and who are the purchasers of gas at the wellhead shall file gas nominations.

(b) The first purchaser shall act as initial nominator. By the fourth day of each month, each initial nominator shall inform its producers of the amount it intends to nominate from each producer. Each initial nominator shall nominate for a total quantity of gas equal to the sum of:

(1) the quantity for which the operator or the initial nominator are the ultimate consumers. This amount will include lease shrinkage, line loss, plant fuel, compressor use, as well as the gas which the initial purchaser may consume at the point of final delivery; and

(2) The total quantity of gas nominated by its downstream purchasers in accordance with the following provisions:

[9 TexReg 4809, September 11, 1984]

(A) all downstream purchasers who take more than 10 MMcf per day shall submit monthly to their initial or first

nominators of gas a downstream purchaser's nomination based on a firm forecast of that purchaser's actual demand;

(B) if a downstream purchaser takes gas from more than one source of supply, that downstream purchaser's nomination shall show expected demand from each source;

(C) written monthly nominations from downstream purchasers shall be kept on file by the initial nominator for commission inspection and shall be filed with the commission on its request;

(3) the remaining quantity of gas which the initial nominator expects to take for direct sale to end-users and any other volumes for which no nomination has been made under paragraph (1) or paragraph (2) of this subsection.

(c) Nominations by a purchaser for a field may not exceed the deliverability to that nominator from that field. The initial nominator of gas shall ratably apportion its nominations among the various fields on a system from which it purchases gas without unjust or unreasonable discrimination. The nomination for each field shall be a consistent percentage of the total deliverability available to the nominator from each field. The nominator shall include the following on the nomination form:

(1) the nomination as a volume of gas in MCF;

(2) the nomination as a percentage of the total deliverability of wells connected to the nominator's system in each field;

(3) the nomination which the nominator filed for that field for the second preceding month (including revisions which were properly filed);

(4) the volume of gas (in MCF) actually taken by the nominator from that field during the second preceding month.

(d) First priority in the nominations for the purchase of gas shall be given to casinghead gas so that gas produced in association with oil production shall not be wastefully vented and oil

production shall not be unnecessarily curtailed. Second priority shall be given to special allowable gas. Third priority shall be given to Statewide Rule 49(b) gas. Refer to § 3.34 of this title (relating to Gas to Be Taken Ratably) for instructions on priority of takes for various categories of gas.

§ 3.31. *Gas Well Allowables.*

(a) General. Allowables of gas wells not currently assigned an allowable will not be made effective:

(1) prior to the well's completion or reclassification date; or

(2) more than 15 days prior to the date all reports or information necessary to the assignment of an allowable are received in the proper commission office. If any report or item of information necessary to the assignment of an allowable is not filed on time, there shall be a one-day allowable reduction for each day the report or information is late.

(b) Changes in gas well allowables.

(1) Changes in allowables of gas wells currently assigned an allowable will be effective on the date of the test or date of the change affecting the well's allowable (when the operator submits special tests or information), provided this is not more than 15 days prior to the date the special test or information is received in the appropriate district office.

(2) With respect to a multicompleted well, the allowable of the second and succeeding zones will be made effective as of the date the multicompletion is approved by the commission or as of the date the last report or item necessary to the assignment of an allowable is received in the commission's office, whichever is the later of the two dates.

(3) When a well is recompleted as a gas well in a different reservoir, any overproduction that has occurred in the old reservoir must be made up before an allowable will be assigned in the new reservoir.

(c) Requirements for gas wells in a field for which an allocation formula has been adopted. In addition to the general requirements set out in subsection (a) and subsection (b) of this section, the following requirements must be met where an allocation formula is applicable before an allowable will be assigned.

(1) If acreage is a factor in the allocation formula, a certified plat showing the acreage to be assigned to the well for proration purposes must be submitted. The plat must be accompanied by a statement that all of the acreage claimed can reasonably be considered productive of gas in that reservoir, and that the distance limitations of the field rules have not been exceeded. If all of the acreage claimed is not contained in a single lease, a certificate of pooling authority must be submitted, stating that the acreage has been pooled. If the distance limitations of the field rules are shown to have been exceeded, the plat must show the number of acres within and beyond the distance limitations. If all of the acreage cannot be considered productive, the plat must also show the productive limit of the acreage. If a plat shows acreage in the proration unit in excess of the maximum number of acres permitted by the field rules, it will not be accepted. The commission shall also be advised if an exception to the distance limitations is desired.

(2) If bottom-hole or reservoir pressure is a factor in the allocation formula, it must be submitted on the appropriate form and must be measured at, or corrected to, the proper datum plane.

(d) Ascertaining allowables by adjustment of gas nominations.

(1) The allocation of allowables to all wells in prorated gas reservoirs will be determined from the nominations submitted, and after consideration at statewide hearing. However, in order to ascertain the reasonable market demand for the gas, nominations for gas shall be adjusted by comparing the latest reported production from the field to the nominaitons filed for that period by purchasers from the field.

(2) The total nominations for gas from prorated wells for any month shall be determined by subtracting the total allowable assigned to nonprorated wells during the months from the total nominations for gas from all wells in the reservoir for that month.

(3) Nothing in this subsection shall be interpreted, however, as binding on the commission to the extent that any adjustment of nominations cannot be made which is necessary to adjust the allowables for gas to an amount equal to market demand as is required of the commission by the statutes.

[9 TexReg 4810, September 11, 1984]

(e) Allowables for prorated and nonprorated wells.

(1) Prorated wells. A prorated well is a well whose allowable is determined by the field allocation formula.

(2) Nonprorated wells. A nonprorated well is a well whose allowable is not determined by the field allocation formula and includes the following types of wells.

(A) A limited well is a well incapable of producing the allowable it would receive under the allocation formula. A limited well shall be assigned an allowable at the rate that the well is capable of producing.

(B) A special allowable well is a well that has been granted a fixed allowable pursuant to commission action. Gas from special allowable wells has priority over prorated gas. A well is classified as a special allowable well based on evidence that producing the well below a specified level will cause loss of the well or loss of recoverable gas.

(3) Allowable adjustments and balancing provisions for limited wells.

(A) A limited well shall not be allowed to accumulate underproduction.

(B) If the most recent production figures reported to the commission show a limited well to be overproduced, the

allowables will be revised to an amount attributable to it under the field allocation formula. If a well's capability to produce, plus its latest overproduction, is less than its formula allowable, it will be assigned its ability to produce, plus its latest overproduction.

(C) If a limited well is assigned an allowable that results in its removal from the nonprorated classification, the underage status of the well shall be reinstated in the amount discontinued at the time the well was placed in the nonprorated category. However, credit will not be given for underproduction attributable to those months when the well was in a nonprorated category, nor can credit be given to underproduction that accumulated prior to the immediately preceding balancing period.

(f) Balancing provisions for overproduction and underproduction of gas for wells completed in nonassociated gas reservoirs. For the purpose of computing and balancing overproduction and underproduction in a gas field in which distribution of allowables to the several wells completed in a common reservoir is governed by special operating rules, the dates 7 a.m., March 1, and 7 a.m., September 1, are to be known as "balancing dates"; and the six months' periods beginning 7 a.m., March 1, and ending 7 a.m., September 1, and beginning 7 a.m., September 1, and ending 7 a.m., March 1, will be considered as separate entities and will be known as "balancing periods."

(1) Underproduction.

(A) If a prorated gas well during the balancing period does not produce as much gas as is allocated to it by the order of the commission, the operator of the well shall be permitted to carry such underproduction forward to the next succeeding balancing period, as future allowable credit to be produced during that period.

(B) The amount of underproduction to be carried forward into any new balancing period as allowed production

during such new balancing period shall consist of the actual underproduction that accrued in the balancing period immediately preceding such new balancing period, and the accumulative well status, as to underproduction, will be adjusted on each balancing date accordingly. Underproduction which accrued prior to the previous balancing period will be canceled. Applications to carry forward underproduction accrued prior to the previous balancing period may be filed with the director of technical hearings. Such applications will be granted only pursuant to hearing with notice to all operators in the field.

(C) Underproduction applicable to any well shall not be made up at a rate in excess of twice the daily average rate required to produce the normal monthly allowable of the well. Under emergency conditions, exceptions to this provision may be granted by the director of the Oil and Gas Division or his delegate.

(D) If a producing well has been accumulatively underproduced on each of two successive balancing dates, the well shall not be assigned a monthly allowable greater than the maximum monthly production from the well during the immediately preceding balancing period; provided, however, the limited allowable assigned to the well may be adjusted to a value not to exceed the allowable applicable to the well under the allocation formula, upon certification to the commission from the operator that such well is producing gas in excess of the limited allowable assigned it.

(2) Overproduction.

(A) Each operator of each gas well, subject to the hereinafter prescribed conditions, may produce the well in excess of the monthly allowable allocated to the well; provided that no well shall in any one month produce in excess of twice the current monthly allowable of the well. Exceptions to this limit may be granted by the commission upon application. No more than two exceptions may be given to a well during one balancing period.

(B) Except where a well is shut-in to make up overproduction (see subparagraph (C) and subparagraph (D) of this paragraph), overproduction existent as of any balancing date shall be made up during the balancing period immediately following, and may be made up at any time during such period.

(C) Any well overproduced as of a balancing date, which was also overproduced on the balancing date immediately preceding and remained overproduced for the entire period between the two balancing dates, shall be shut in until the overproduction, existent as of the later of such two balancing dates, is made up, unless exception is granted as provided for in subparagraph (D) of this paragraph.

(D) The operator of a well which, under the provisions of subparagraph (C) of this paragraph, would be required to be shut in, may request authority to produce the well at a reduced rate. Authority to produce at a reduced rate until the end of the balancing period may be granted administratively by the director of proration if no protest is received from other operators in the field. If a protest is received, reduced rate authority may be granted only pursuant to hearing. Notice of the hearing will be given to all operators in the field. If, after consideration of the evidence submitted at the hearing, the commission finds that the well would be damaged if shut in, the commission may allow the overproduction charged against it to be made up at a lesser rate than it would be made up if the well were shut in. Production of the [9 TexReg 4811, September 11, 1984] well in any one month may not exceed half the normal rate.

This agency hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's authority to adopt.

Issued in Austin, Texas, on August 28, 1984.

TRD-849090 Walter Earl Lilie
Special Counsel
Railroad Commission of Texas

Proposed date of adoption:

November 5, 1984
For further information, please call (512) 445-1186.

16 TAC § 3.34

The Railroad Commission of Texas proposes new § 3.34, concerning ratable taking of natural gas.

The new section, if adopted, will replace § 3.91, which is simultaneously proposed for repeal. The proposed new section alters the commission's regulation of ratable taking to make it responsive to changes in the gas industry.

Patrick Thompson, Oil and Gas Division legal examiner, has determined that for the first five-year period the rule will be in effect there will be no fiscal implications for state or local government or small businesses as a result of enforcing or administering the rule.

Mr. Thompson also has determined that for each year of the first five years the rule as proposed is in effect the public benefit anticipated as a result of enforcing the rule as proposed is increased understanding of the rule, greater flexibility in the purchasing and transporting of natural gas, and increased accessibility of gas and transportation facilities. The anticipated economic cost to individuals who are required to comply with the rule as proposed will not vary from that under the rule currently proposed for repeal.

Comments on the proposal may be submitted to Patrick Thompson, Legal Section, Oil and Gas Division, Railroad Commission of Texas, P.O. Drawer 12967, Austin, Texas 78711.

A public hearing on the proposed new section is scheduled in Room 221, Railroad Commission of Texas Building, 1124 IH 35 South, Austin, at 9 a.m. on Monday, October 22, 1984. Written comments will be accepted through October 23, 1984.

The new section is proposed under the Texas Natural Resources Code, § 111.083 and § 111.090, which provides the Railroad Commission of Texas with the authority to adopt rules to prevent discriminatory purchasing or taking of natural gas.

§ 3.34. *Gas to be Taken Ratably.*

(a) This rule is promulgated to promote and maintain ratable production of natural gas and to protect correlative rights through the enforcement of ratable taking by natural gas pipelines. Enforcement of this rule is also intended to prevent the exercise of monopoly power by natural gas pipelines. A purchaser or transporter of gas from gas wells may not discriminate between different wells in the same field, nor may it discriminate unjustly or unreasonably between wells in separate fields. The provisions of this rule requiring ratable taking of gas apply to takes from all gas wells on a pipeline system, excluding Statewide Rule 49(B) wells and special allowable wells. The taking of casinghead gas is also excluded. Subsection (g) of this section governs takes from the excluded wells.

(b) Purchasers of natural gas, including pipelines and their subsidiaries or affiliates, which purchase gas from different wells in the same field shall purchase the same percentage of allowable from all such wells in the field which offer their gas for purchase. Purchases from limited wells shall be in accordance with subsection (e) of this section. When purchasing from split stream wells, this percentage should be applied to that portion of the total allowable dedicated to the particular purchaser on the commission Form P-4, and not to the total allowable for the well. If takes from different wells in the same field become nonratable, the purchaser shall take commission-assigned underproduction and overproduction into consideration in establishing an appropriate pattern of takes to restore ratability.

(c) Purchasers of natural gas, including pipelines and their subsidiaries or affiliates, which purchase gas from more than one field must take a consistent percentage of the aggregate deliverability to that purchaser from each field, unless the purchaser can demonstrate a just and reasonable basis for discriminating between fields.

(d) A pipeline which transports gas from producing wells in a field may not discriminate between wells in the field which offer their gas for transport. Pipelines which transport gas for

hire shall make their transportation facilities available on a fair and equitable basis to all wells in the field which offer their gas for transport.

(e) Purchases from limited wells (wells incapable of producing the full allowable they would receive under the allocation formula, designated by the commission with a # or @ symbol) shall not be reduced until all other wells in the field connected to that pipeline are reduced to the level at which that limited well can produce. Below that point, purchases from all prorated wells and limited wells should be reduced ratably.

(f) Operators shall apportion purchasers' take requests ratably to all wells in each field without discrimination as provided in subsections (a)-(d) of this section.

(g) Purchasers of gas shall satisfy their demand for gas by taking gas, up to the assigned allowable or limit for each well, from the following categories, in order:

(1) all casinghead gas and/or "garbage gas" connected directly to the pipeline;

(2) all gas from wells which have been assigned special allowables by the commission;

(3) gas from wells subject to Statewide Rule 49(b), but only to the extent of one full allowable in the case of multiple 49(b) wells;

(4) gas from prorated wells, including limited wells (see subsection (d) of this section).

(h) Any producer who is denied the opportunity to produce a ratable share of gas by a pipeline or purchaser, in violation of this rule, may file a complaint with the commission and request an order to end the discriminatory practices.

(i) If a producer fails to comply with a purchaser's request to ratably reduce production after reasonable [9 TexReg 4812 September 11, 1984] notice by the purchaser, the purchaser

may file a complaint with the commission and request an order directed at the producer to reduce production to ratable levels.

This agency hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's authority to adopt.

Issued in Austin, Texas, on August 28, 1984.

TRD-849087 Walter Earl Lilie
Special Counsel
Railroad Commission of Texas

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For further information, please call (512) 445-1186.

Miscellaneous

16 TAC § 3.91

(Editor's note: The text of the following rule proposed for repeal will not be published. The rule may be examined in the offices of the Railroad Commission of Texas, 1124 IH 35 South, Austin, or in the Texas Register office, Room 503E, Sam Houston Building, 201 East 14th Street, Austin.)

The Railroad Commission of Texas proposes the repeal of § 3.91, concerning the ratable taking of natural gas. The repeal is being replaced by simultaneously proposed new § 3.34.

Patrick Thompson, Oil and Gas Division legal examiner, has determined that for the first five-year period the repeal will be in effect there will be no fiscal implications for state or local government or small businesses as a result of the repeal.

Mr. Thompson also has determined that for each year of the first five years the repeal is in effect the public benefit anticipated as a result of the repeal is the accommodation of the adoption of the proposed new section. The merits of the new section are discussed in a separate proposal. The anticipated economic cost to individuals who are required to comply with

the new rule will not vary from the cost under the existing section in any definable way.

Comments on the proposal may be submitted to Patrick Thompson, Legal Section, Oil and Gas Division, Railroad Commission of Texas, P.O. Drawer 12967, Austin, Texas 78711.

The repeal is proposed under the Texas Natural Resources Code, § 111.083 and § 111.090, which provides the Railroad Commission of Texas with the authority to prevent, by regulation, discriminatory purchasing or taking of natural gas.

§ 3.91. *Gas Market Demand, Allocation of Gas Well Allowables, and Ratable Take Between Gas Wells and Gas Fields.*

This agency hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's authority to adopt.

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TRD-849089 Walter Earl Lilie
Special Counsel
Railroad Commission of Texas

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